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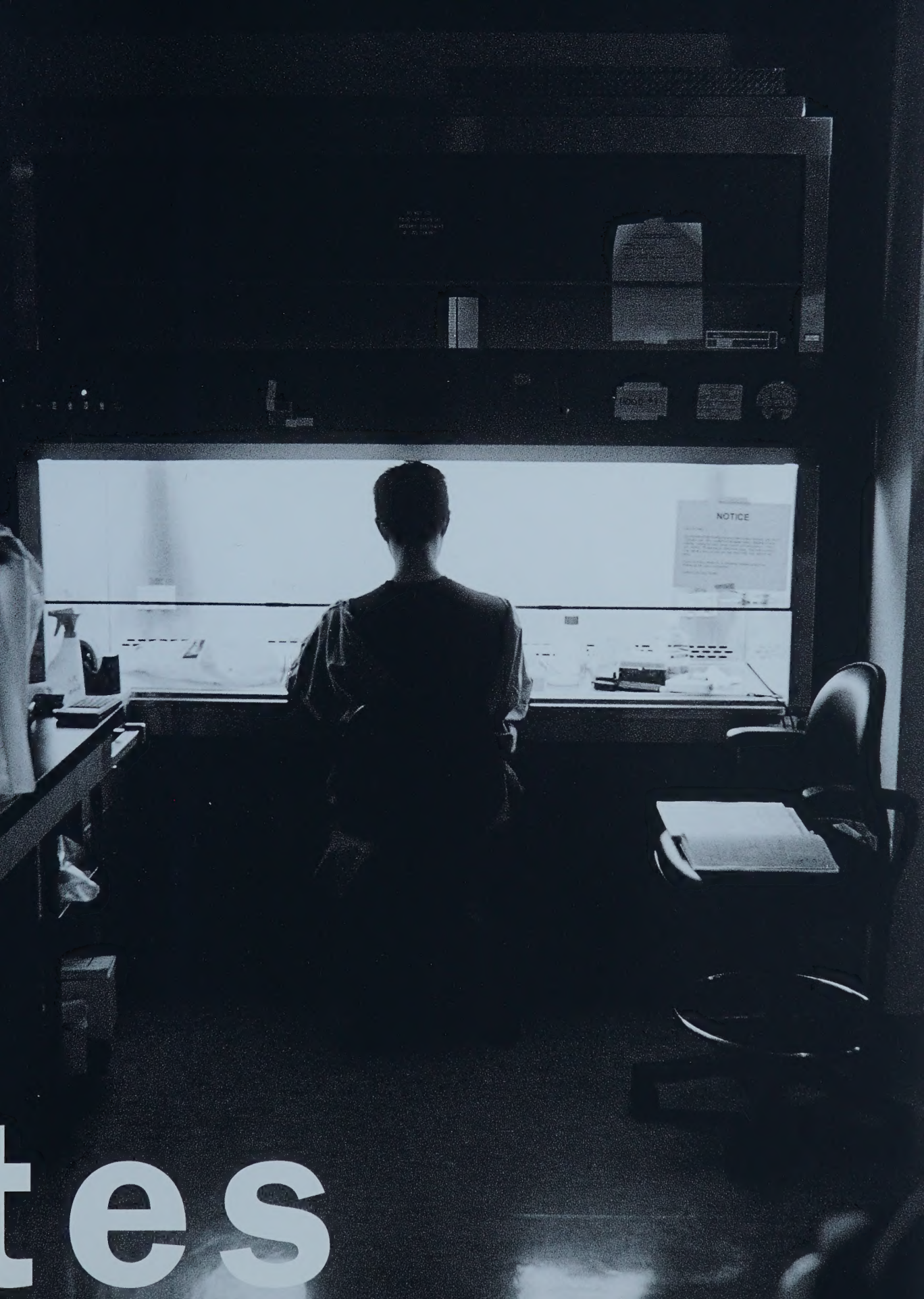

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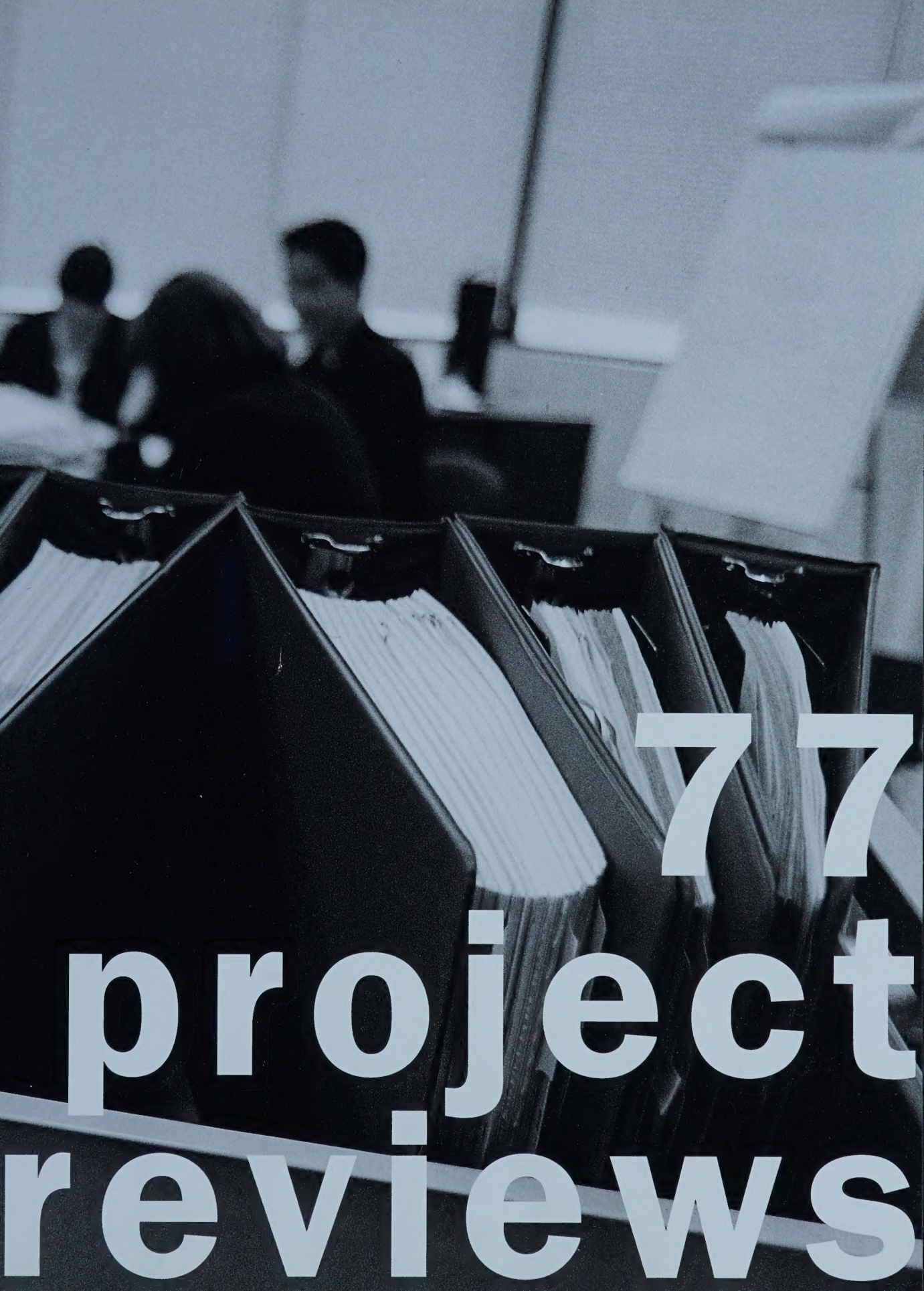

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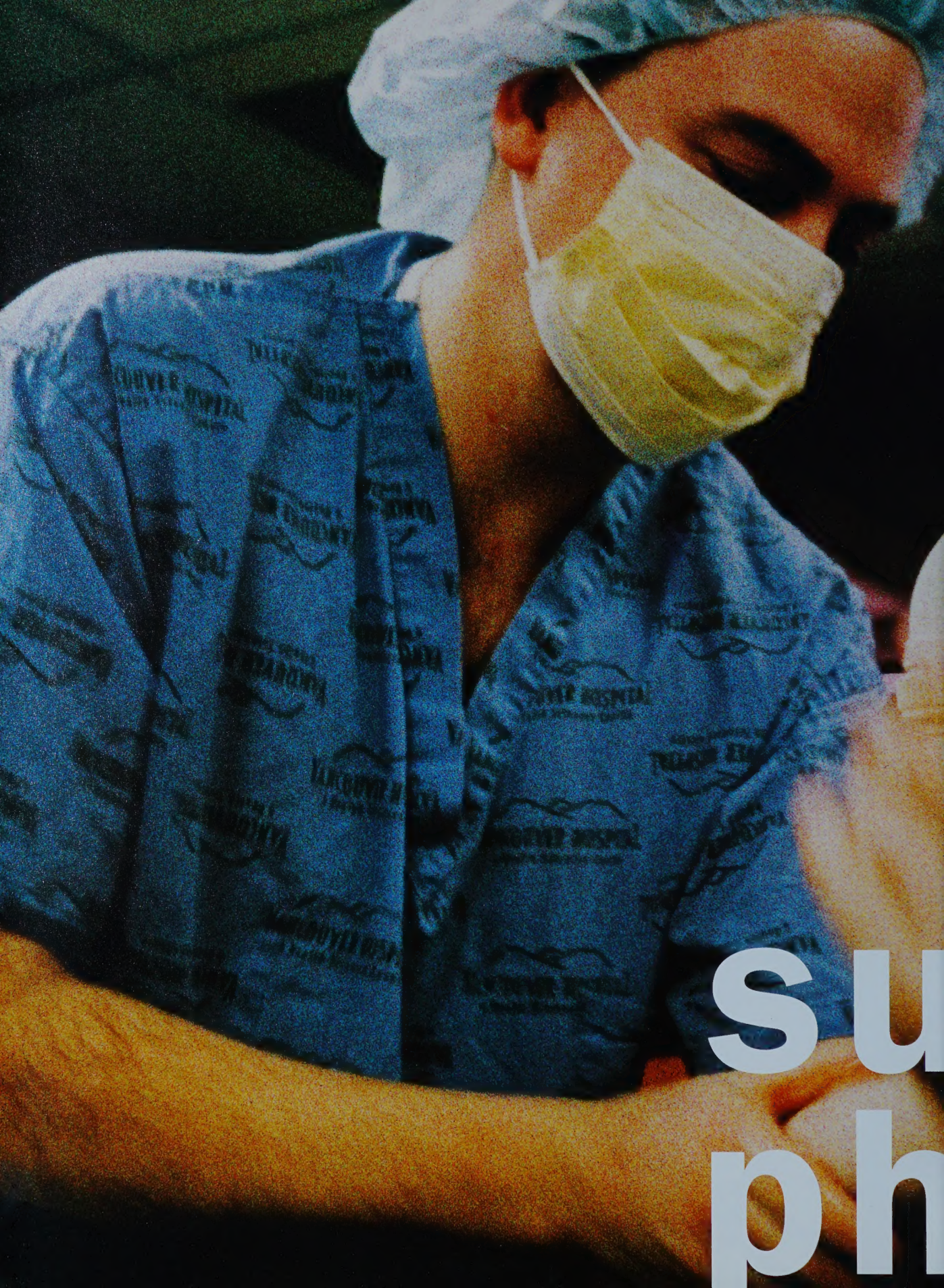
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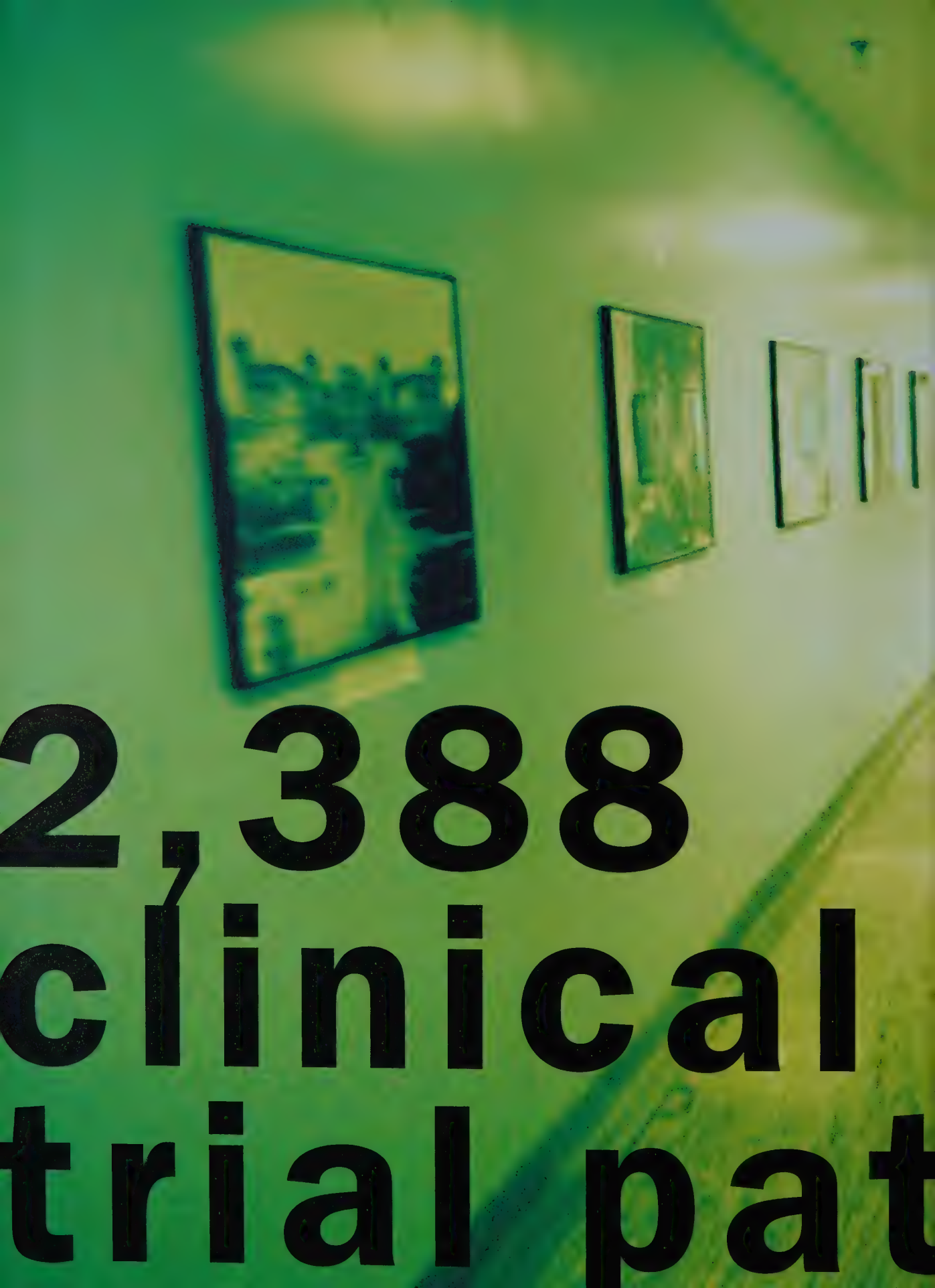
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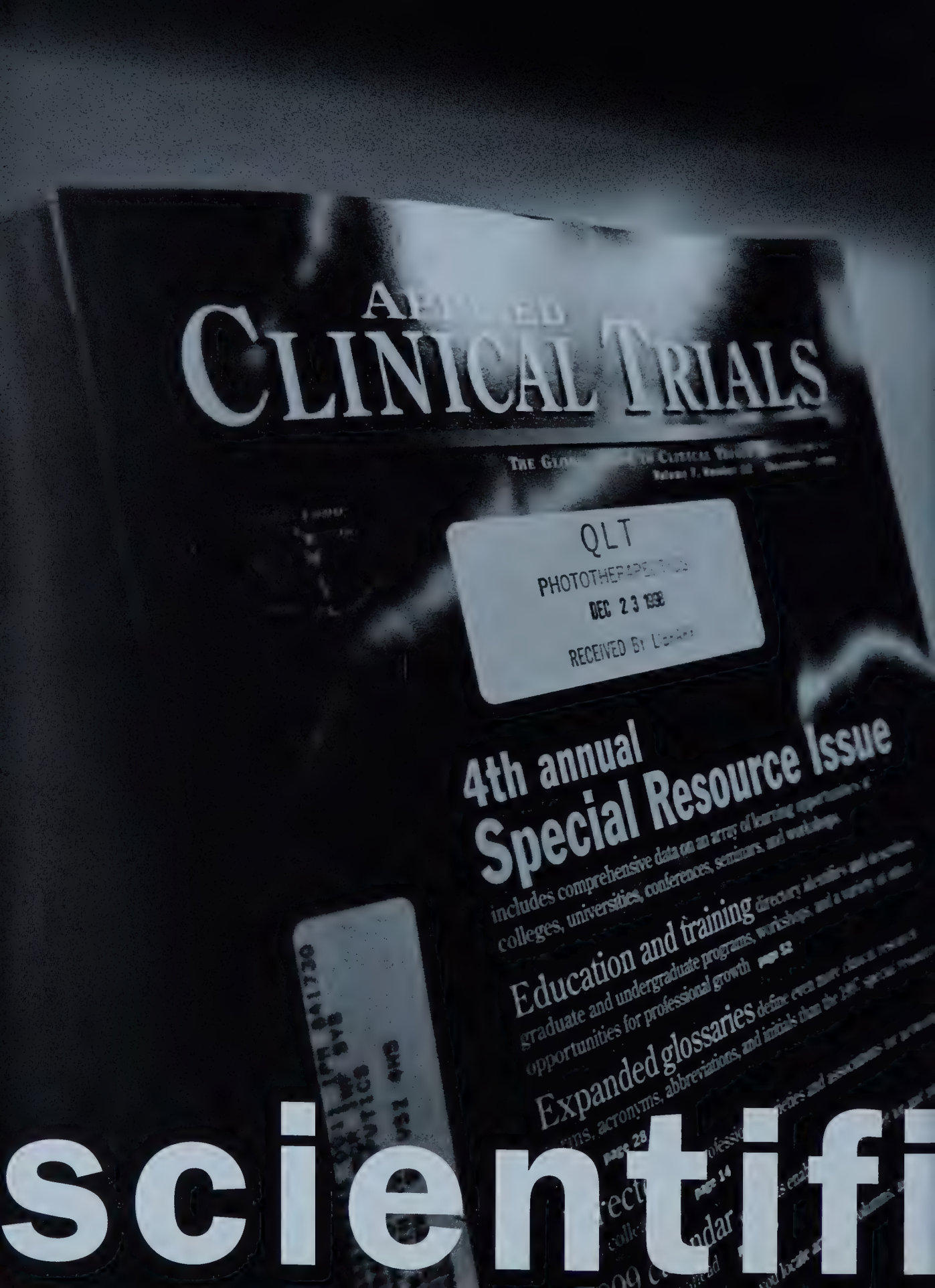
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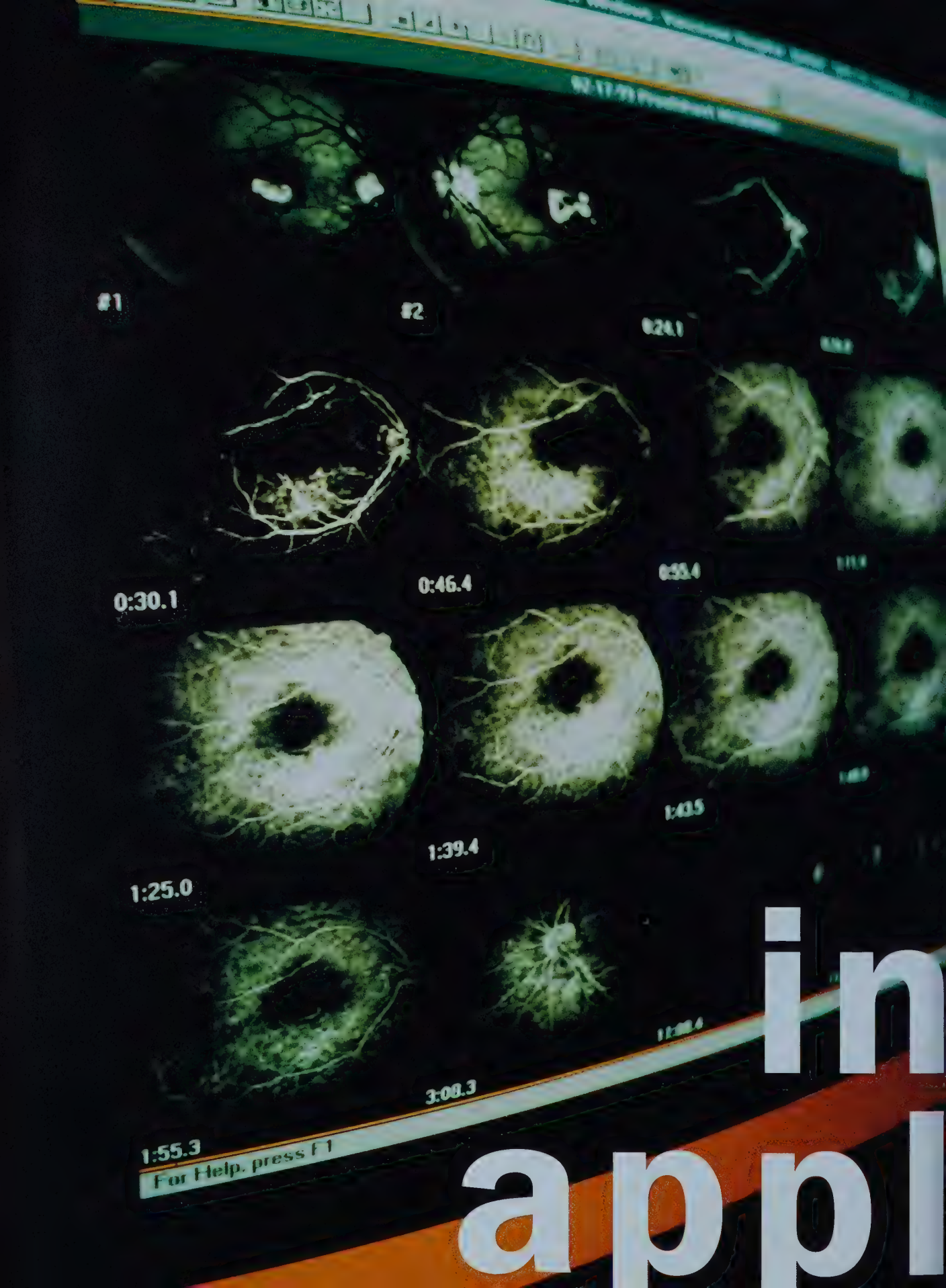
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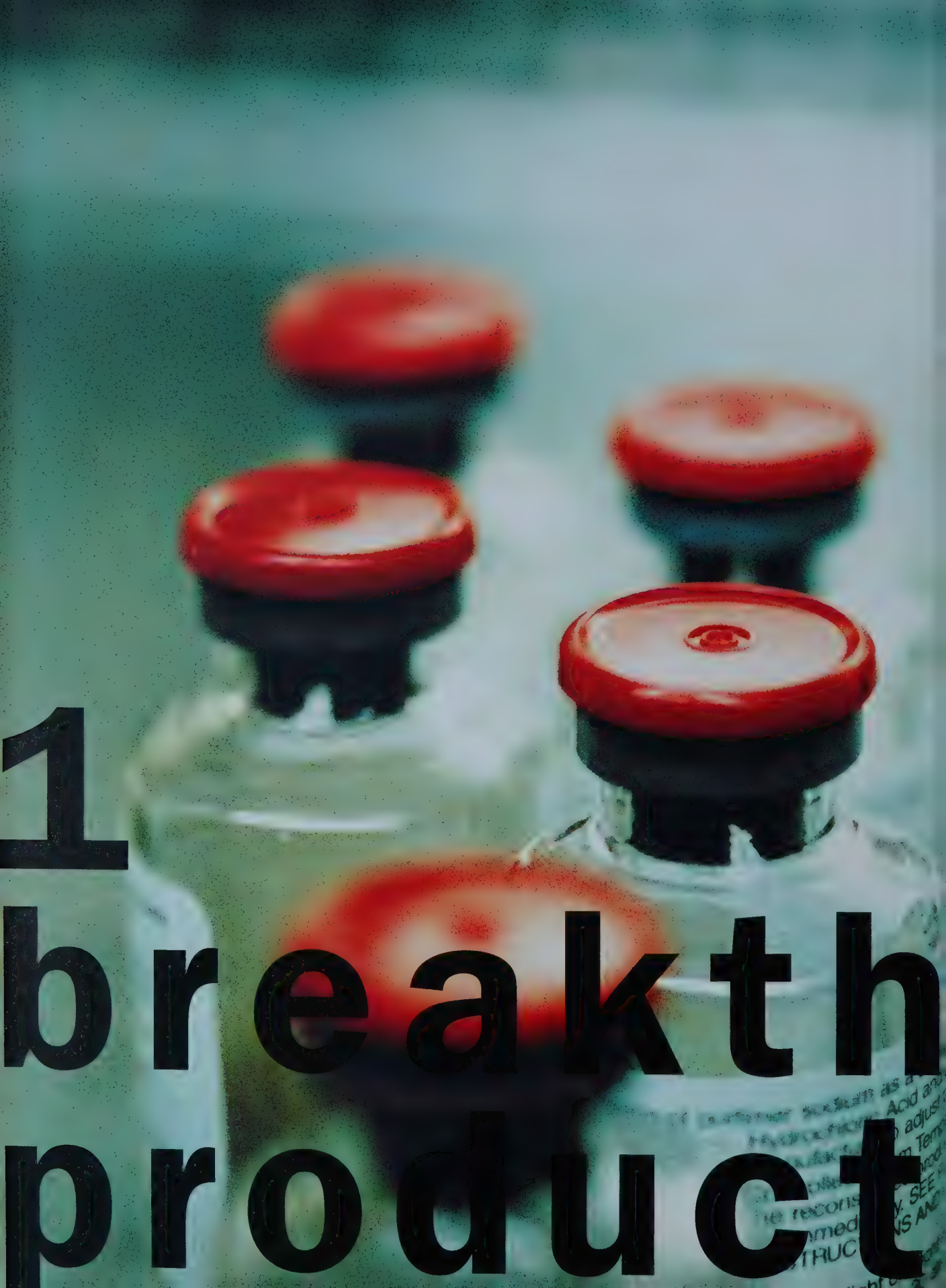
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And now we begin...

Corporate Profile

QLT PhotoTherapeutics Inc. (QLT) is a world leader in the development and commercialization of proprietary pharmaceutical products for use in photodynamic therapy, an emerging field of medicine utilizing light-activated drugs in the treatment of disease. QLT's innovative science has advanced photodynamic therapy beyond applications in cancer towards potential breakthrough treatments in ophthalmology, autoimmune and cardiovascular disease.

QLT's portfolio of products include PHOTOFRIN® (porfimer sodium), the world's only approved photodynamic therapy drug, used in the treatment of various cancers throughout North America, Japan and Europe; and Visudyne™ (verteporfin), a therapy in final stages of testing to treat the wet form of age-related macular degeneration (AMD), the leading cause of blindness in people over the age of 50.

Selected Financial Data

(In millions of dollars, except per share information)	1998 $ Cdn.	1998 $U.S.	1997 $ Cdn.	1997 $U.S.	1996 $ Cdn.	1996 $U.S.
Royalties on product sales	2.0	1.3	1.2	0.8	0.7	0.5
Revenue from collaborative arrangements	—	—	2.8	2.0	9.5	7.0
Interest and other income	5.6	3.8	6.4	4.6	3.3	2.4
Research and development expenses	23.9	16.1	19.2	13.9	11.5	8.5
Net loss	24.1	16.3	16.7	12.1	4.7	3.5
Net loss per share	0.90	0.61	0.64	0.46	0.19	0.14
Weighted average shares outstanding	26.7		26.0		24.5	
Cash, cash equivalents and investment securities	78.2	52.7	89.8	62.9	97.2	71.5
Total assets	103.2	69.6	101.2	70.9	112.2	82.5
Shareholders' equity	95.1	64.1	94.8	66.5	108.9	80.1
Shares outstanding at end of year	27.3		26.1		25.9	
Employees	194		147		115	

Certain Statements in this Annual Report constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company, or industry results, to be materially different from any future results, performance, or achievements expressed or implied by such forward-looking statements. Such factors include, among others, risks associated with the commercialization of PHOTOFRIN® and verteporfin; uncertainties relating to product development; the Company's history of operating losses and uncertainty of future profitability; uncertainty of access to additional capital; rapid technological change and competition; uncertainty regarding patents and proprietary rights; product liability claims and insurance; manufacturing uncertainties; anti-takeover provisions; uncertainty of pricing and reimbursement; no assurance of regulatory approval; government regulation; volatility of common share price and dependence on corporate relationships, all as described in the Company's annual information form on Form 10-K.

To Our Shareholders

And so we begin, indeed – to claim our role on the global stage as a premiere biopharmaceutical company with a breakthrough drug that has the potential to enrich the lives of hundreds of thousands of people all over the world.

The path that brought us to this level started with an exploration into the applications of photodynamic therapy nearly 15 years ago and has led us to the successful development of Visudyne™ – a breakthrough product used in the treatment of wet age-related macular degeneration (AMD), which afflicts nearly 500,000 patients worldwide every year.

Many factors converged to bring us to this pivotal juncture and to help QLT's evolution into a strong commercial entity with a clear mission: the crucial decision to move beyond cancer and explore the uncharted therapeutic area of AMD; the invaluable insight and experience gained throughout the demanding regulatory process with PHOTOFRIN®; the 75 product candidates from which we identified Visudyne™; the unwavering support of 2,388 patients and 258 physicians who participated in our clinical trials.

Further, our partnerships with pharmaceutical leaders such as CIBA Vision and Sanofi have provided us with the necessary infrastructure to bring our products to the marketplace.

But perhaps the single-most important factor in our success over the past year – indeed throughout QLT's history – has been our people. Fifteen years of experience and growth, through successes and setbacks alike, have culminated in a world class team with expertise and knowledge in every aspect of drug development from design through clinical testing to regulatory approval and marketing. Some of these individuals you will meet in profile throughout this report; many of them experts in their respective fields; each and every one of them singularly committed to QLT's success.

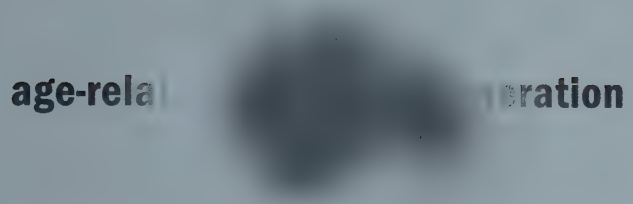
The value of this critical mass of intellectual capacity cannot be understated, for while we have attained a significant achievement with the development of Visudyne™, the bar is undoubtedly higher and QLT has been catapulted into a different league.

Visudyne™ promises to be the largest success in QLT's history to date – we are committed to ensuring it is not our last. We will devote tremendous efforts to securing approval and bringing the product to market over the next twelve months. But even as Visudyne™ reaches market and begins generating revenue, we must maintain our long-term commitment to research and development. We intend to explore growth opportunities through new applications of photodynamic therapy and the acquisition or in-licensing of complementary technologies.

Maximizing these opportunities is the key to future success, for each new opportunity contains limitless potential to grow in new directions, to expand our existing knowledge base, to make a significant societal impact – to achieve new successes.

And therein lies the true value of new beginnings.

The development of wet AMD results in a total loss of central vision in as little as two years.



Business Review

Ophthalmology **Clearly, our most important achievement last year was the successful 12 month analysis of our two year TAP (Treatment of AMD with Photodynamic therapy) Investigation.**

Together, the dry and wet forms of AMD affect millions of people worldwide. The wet form of AMD is less prevalent than the dry form, but accounts for 90% of the vision loss associated with the disease. It is characterized by the growth of abnormal blood vessels across the central part of the retina, called the macula. Because these vessels don't mature properly, they begin to leak, which over time results in photoreceptor damage and scar tissue. The entire progression of the disease varies from patient to patient, but the majority lose total central vision in as little as two years.

Worldwide, approximately 500,000 patients develop wet AMD annually – about the same number of patients who develop breast cancer each year – and this number is expected to grow as the population ages. No treatment options currently exist for the vast majority of patients, for whom this devastating disease means loss of independence and the ability to carry out simple daily activities such as reading, shopping and watching television.

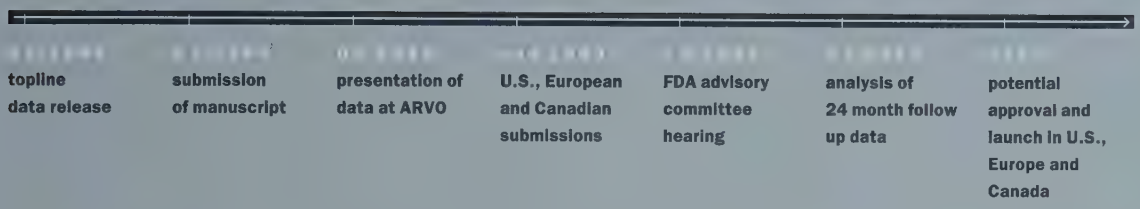
Visudyne™ therapy is a simple procedure designed to stop the progression of the disease by selectively closing the leaky vessels. It is an outpatient procedure that can be repeated up to every three months and takes less than a half-hour.

Initial results from the two pivotal double-masked, placebo-controlled trials that comprised the TAP Investigation, showed that patients treated with Visudyne™ therapy were 34% more likely to have stable or improved vision compared to placebo-treated patients, where "stability" was defined as a loss of less than three lines of vision on a standard eye chart. Specifically, 61.4% of treated patients lost less than three lines of vision compared to 45.9% of patients treated with placebo. These results, which were based on 609 patients from 22 sites throughout North America and Europe, were statistically significant.

Although the objective of Visudyne™ therapy is to stop the progression of AMD and the resulting loss of vision, approximately one out of every six patients treated with Visudyne™ actually experienced an improvement of one or more lines lasting one year.

Further confirmation of the effectiveness of Visudyne™ was demonstrated by additional endpoints that were statistically significant based on data from both studies. These endpoints included severe vision loss, contrast sensitivity, and physiological measurements such as reduction in lesion size and amount of leakage.

Estimated timing of milestones relating to our AMD program



Safety data were equally encouraging – and of particular importance given the average age of patients in the trials was 75. Visudyne™ was found to be very well tolerated. The most common treatment-related adverse events included injection site reactions, which occurred in 9% more treated patients compared to placebo, and a transient loss of vision. This latter event was a short term effect occurring in 2% more treated patients compared to placebo. Further, only 2% of patients receiving treatment experienced a photosensitivity reaction within the first 24 hours.

Based on these positive results and our desire to make this therapy available to patients as soon as possible, we and our partner CIBA Vision – the eye care unit of Novartis AG – have decided to proceed to file for approval in the U.S., Canada, and Europe prior to completing the 24 month follow up. The U.S. Food and Drug Administration (FDA) has agreed to base their review on the initial data, provided the trial is completed as originally planned. Pending a submission in mid 1999 and subsequent approval, we hope to make Visudyne™ therapy available to patients in early 2000.

During 1999, we will work with CIBA Vision on commercial issues to ensure adequate product supply following launch, reimbursement, laser placements, and physician training.

To protect our leadership position in ophthalmology, in 1998 we completed patient recruitment for two additional Phase III trials to study the effectiveness of Visudyne™ therapy in patients with early AMD who were not eligible for the initial TAP Investigation, as well as a group of patients with a similar but distinct condition resulting from progressive near-sightedness, known as pathologic myopia. This latter condition, which occurs at a much younger age, represents an additional 50,000 new patients per year. To grow our ophthalmology franchise, we will begin to evaluate the potential of photodynamic therapy for other ophthalmic conditions.

Pending approval, many factors will entrench Visudyne™ as the treatment of choice for wet AMD. It will be the first and only photosensitizer available to patients for at least two years following market launch; the lasers used to activate Visudyne™ cannot be used with any other photosensitizer; rapid uptake of Visudyne™ by blood vessels results in procedures that take less than a half-hour to administer, and; fast clearance causes photosensitivity to wear off within 24 hours. Furthermore, an equal profit-sharing arrangement with CIBA Vision should mean strong future revenue growth for QLT.

Oncology The past year was a fruitful one for PHOTOFRIN, particularly in the U.S. where we obtained two additional approvals and saw a steady increase in usage. U.S. marketing efforts by our oncology partner, Sanofi Pharmaceuticals, Inc., made up the bulk of worldwide PHOTOFRIN sales of Cdn.$8.8 million dollars – an increase of 83% over 1997.

Early in 1998, the FDA approved PHOTOFRIN as a treatment for early-stage lung cancer. This landmark decision represented the first time that the technology was approved in North America as a "curative" treatment – thereby providing the greatest benefit to patients.

Following a successful advisory committee hearing in September, PHOTOFRIN's label was further expanded by the FDA in December to include the palliative treatment of advanced lung cancer. This approval substantially increases the potential market for PHOTOFRIN and should contribute to continued sales growth in 1999. Efforts are also underway to introduce a compact, less expensive diode laser to the North American marketplace for use in oncology which will likely expand the number of laser sites. At the end of 1998, 75 cancer centers in the U.S. were performing photodynamic therapy with PHOTOFRIN.

European efforts are progressing as approvals in additional countries are received. Already in early 1999, PHOTOFRIN was approved in both the U.K and Finland for the palliative treatment of lung and esophageal cancer. Submissions are pending in nine other European countries, as well as Canada and Iceland.

To further increase our oncology franchise, last year we initiated two clinical trials in oncology – a Phase III study using PHOTOFRIN to treat Barrett's esophagus and a Phase II study using verteporfin for non-melanoma skin cancer.

Barrett's esophagus is a pre-cancerous condition which occurs when the lining of the esophagus converts to stomach-type tissue in response to chronic acid reflux. The rise in esophageal cancer has been attributed to the increasing prevalence of Barrett's esophagus, which afflicts approximately two million people throughout North America. For those patients with advanced disease, other than surgical removal of the esophagus, there are currently no approved treatments for this condition.

Approximately 200 patients with high-grade dysplasia – the final stage of abnormal tissue transformation – are being recruited at roughly 35 sites in North America and Europe. Patient recruitment will be completed in 1999 with initial results expected in early 2000.

Roughly one in six patients diagnosed with non-melanoma skin cancer are non-candidates for surgery because of the location of their tumor or because they have multiple tumors. We are developing verteporfin as an alternative for these patients. Early studies have shown treatment with photodynamic therapy to result in complete response rates with a cosmetic outcome superior to surgery. In addition, we have developed a multi-head LED light source to facilitate the treatment of patients with multiple tumors. We plan to complete our Phase II study this year and initiate a pivotal trial in 2000.

Autoimmune Disease Our ability to develop innovative applications for photodynamic therapy has led to promising research in the area of autoimmune disease. Using a different approach from that used in cancer and ophthalmology, we are able to down-regulate specific cells of the immune system following low dose injection of a photosensitizer and whole body illumination. Since immune cells travel throughout the body, once activated, they assert their effect systematically. Because of the selective nature of the treatment, the entire immune system is not compromised, as is the case with many existing therapies.

Dr. Julia Levy, Ph.D
President and Chief Executive Officer

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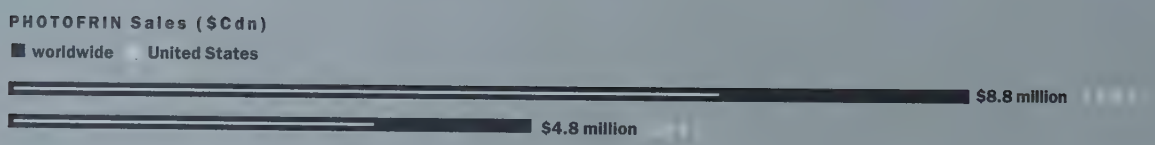

Financial Highlights

In a prudent move last year, we increased our cash position by completing a public offering of one million shares in July. Despite poor market conditions, we felt it was strategically important to increase our flexibility as we began preparations for the commercialization of Visudyne™. As a result, our current financial position remains strong, with cash resources totaling $78 million.

Revenues for 1998 totaled $7.6 million and included $2 million in royalties from worldwide PHOTOFRIN sales of $8.8 million. A 24% increase in research and development spending – to $23.9 million – brought total 1998 expenses to $31.6 million, up from $27 million in 1997. Total costs are expected to increase further in 1999 as our major Phase III programs continue. QLT posted a net loss of $24.1 million or $0.90 per share in 1998.

QLT's stock performed well throughout 1998 despite volatile conditions for the sector. Investors remained both cautious and selective, favoring companies in late stage development with reduced risk and substantial market opportunities. QLT was well rewarded by the investment community as it met the above criteria with positive Phase III results for AMD.

The past 12 months have been a period of tremendous learning and expansion for QLT. Visudyne™ signals the start of a new era of growth and opportunity. Part of this growth will be fueled by our existing business, as evidenced by the steady expansion in our oncology division. Over the long term, developments in the pipeline will see new applications for photodynamic therapy and beyond – we've already begun investigating the potential for a number of debilitating disease areas including psoriasis and rheumatoid arthritis. And with each opportunity comes the freedom to explore new heights as a world-class biopharmaceutical company and the potential to significantly improve the quality of life for millions of patients around the world.

This is what truly drives us to succeed. And then to begin again.

On behalf of the entire team at QLT, I'd like to extend our sincere gratitude to our shareholders for their support, commitment and trust.

JULIA LEVY, Ph.D., D.SC., F.R.S.C.
President and Chief Executive Officer
March, 1999

Photodynamic therapy Photodynamic therapy is a platform technology that utilizes light-activated drugs to treat a wide range of medical conditions. Any disease associated with rapidly growing tissue, including the formation of abnormal blood vessels, can potentially be treated with this technology. QLT's innovative science has advanced photodynamic therapy beyond applications in cancer towards potential breakthrough treatments in ophthalmology, autoimmune and cardiovascular disease.

Treatment with photodynamic therapy consists of a two-step process beginning with administration of the drug, or "photosensitizer", by intravenous injection. While circulating in the bloodstream, the drug attaches to molecules called lipoproteins. Because cells undergoing rapid proliferation require a greater amount of lipoproteins than non-dividing cells, the drug is delivered more quickly and in higher concentrations to these types of cells.

Once the concentration of drug reaches appropriate levels in target cells, it is activated with a pre-calculated dose of light at a particular wavelength. The activated drug subsequently causes the conversion of normal oxygen found in tissue to a highly energized form called "singlet oxygen". The singlet oxygen, in turn, causes cell death by disrupting normal cellular functions. Neither the drug nor the light exert any effect until combined.

Because the light is shone directly at the targeted tissue and the drug accumulates preferentially in these cells, photodynamic therapy results in a highly selective treatment. Selectivity is advantageous because it reduces damage to normal surrounding tissue, allowing for retreatment. As a minimally invasive procedure, photodynamic therapy can be performed in a physician office or on an out-patient basis.

Dr. John North, Ph.D
Vice President, Scientific Affairs and Chief Scientific Officer

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Dr. John North, Ph.D
Vice President, Scientific Affairs and Chief Scientific Officer

Dr. North joined QLT in 1998 with experience in all stages of pharmaceutical and device development, including pre-clinical research, commercial evaluation and project management.

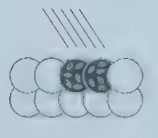
In his current role, Dr. North coordinates the oncology business group and the development of QLT's third photosensitizer, QLT 0074, while leading the pre-clinical pharmacology and toxicology groups which include more than 20 scientists. The strengths of this talented group – formerly headed by Dr. Julia Levy – have led to major innovations at QLT, including the evolution of photodynamic therapy beyond cancer and into promising new disease areas such as ophthalmology and immune modulation.

Through the evaluation of new compounds generated by the Technology Development group, Dr. North's team represents the engine that drives the future growth of QLT. Drawing on his expertise in project management, Dr. North is currently formalizing a structure for the allocation of resources and coordination of project activities.

"As QLT continues to evolve, it's increasingly important that we maintain an environment that nurtures creativity. While we recognize that Visudyne™ therapy represents an enormous opportunity, it will be imperative that we continue to generate new products and applications for our technology."

a photosensitizer is injected into the bloodstream, attaching to lipoproteins

lipoproteins carry the photosensitizer to target cells



photosensitizer is activated by light, resulting in disruption of biochemical processes in target cells

target cells are destroyed, leaving surrounding cells intact

Devices **QLT ensures the availability of state-of-the-art light sources and delivery systems by forming alliances with leading medical device companies for the co-development and promotion of dedicated photodynamic therapy lights and related devices. Today, companies such as Coherent Medical Group, Diomed, Laserscope and Zeiss produce the devices used to activate QLT's products.**

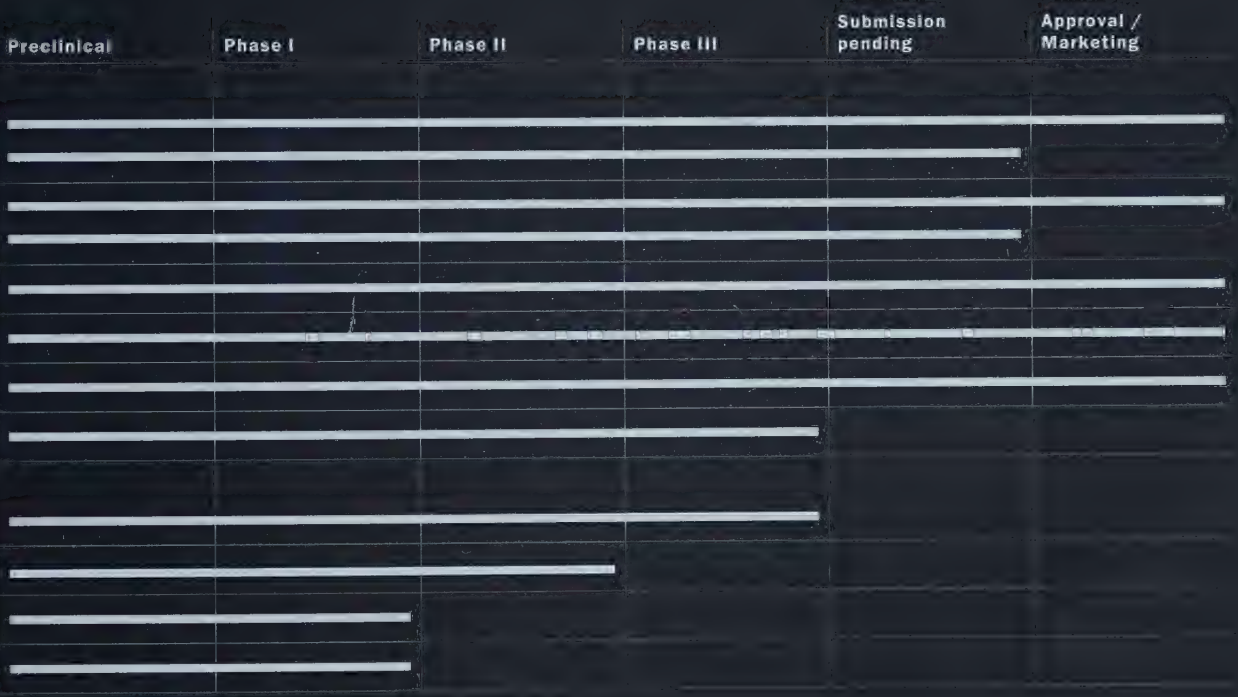
The type of light source used varies depending on the indication being treated. When treating internal conditions such as cancer, a fiber optic is used to deliver light to the treatment site from either an argon-ion dye pumped laser or a diode laser. In ophthalmology, diode laser light is shone through the slit lamp of a microscope into the patient's eye. In the case of autoimmune conditions, patients stand in a whole body light box containing fluorescent lights of an appropriate wavelength.

Future advancements in device technology resulting in the availability of better, lower cost light systems will undoubtedly contribute to the further establishment of photodynamic therapy.

Product/ Indication	Jurisdiction
PHOTOFRIN	
Esophageal cancer	U.S., Canada, Japan, France, Netherlands, U.K., Finland Italy, Ireland, Spain, Portugal, Belgium, Denmark, Sweden, Greece, Norway, Iceland
Lung cancer	U.S., Japan, France, Netherlands, Germany, U.K., Finland Canada, Italy, Ireland, Spain, Portugal, Belgium, Denmark, Sweden, Greece, Norway, Iceland
Bladder cancer	Canada
Gastric cancer	Japan
Cervical cancer/dysplasia	Japan
Barrett's esophagus	U.S., Canada, Europe
verteporfin	
Macular degeneration	U.S., Canada, Europe
Skin cancer	
Psoriasis	
Rheumatoid arthritis	

QLT Partnerships

An integral part of QLT's business strategy is to form strategic alliances for the international marketing and distribution of its products. Through joint management committees, QLT works closely with its partners to maximize commercial potential through product development and marketing activities.



Therapeutic area	Product	Partners	Jurisdiction
Oncology (includes cancerous and pre-cancerous conditions)	PHOTOFRIN, verteporfin	Sanofi Pharmaceuticals, Inc.	U.S., Caribbean
		Beaufour Ipsen	Europe
	PHOTOFRIN	Wyeth Lederle Japan, Ltd.	Japan
		Ligand Pharmaceuticals Inc.	Canada
Ophthalmology	Visudyne™	CIBA Vision, the eye care unit of Novartis AG	Worldwide
Autoimmune disease	QLT 0074	currently unpartnered	
Cardiovascular disease	PHOTOFRIN	Arterial Vascular Engineering, Inc.	Worldwide

The following information should be read in conjunction with the Company's 1998 consolidated financial statements and related notes included therein, which are prepared in accordance with generally accepted accounting principles in Canada (Canadian GAAP). These principles differ in certain respects from generally accepted accounting principles in the United States (U.S. GAAP). The differences as they effect the financial statements of the Company are described in Note 11 to the Company's audited 1998 consolidated financial statements. All amounts following are expressed in Canadian Dollars unless otherwise indicated.

Overview

Since its inception in 1981, the Company has been engaged primarily in the research and development of proprietary pharmaceutical products and only recently has generated initial royalty revenues from the commercial sale of such products. The Company has not earned any profits since its inception and expects to incur additional operating losses over the next few years due to continued requirements for research and development, preclinical and clinical testing and regulatory activities and until further and initial marketing approvals for PHOTOFRIN® (porfimer sodium) and Visudyne™ (verteporfin), are obtained and significant revenues realized therefrom.

The Company has incurred increasing annual operating expenses and, with the forthcoming commercialization of Visudyne™, the Company expects such trends to continue. The Company has incurred annual operating losses since its inception in 1981, and the transition of the Company to profitability will be dependent upon the commercial success of Visudyne™. As of December 31, 1998, the Company had an accumulated deficit of $140.7 million.

Results of Operations

For the year ended December 31, 1998, the Company recorded a net loss of $24.1 million or $0.90 per common share. These results compare with a net loss of $16.7 million, or $0.64 per common share, and $4.7 million, or $0.19 per common share, for the years ended December 31, 1997 and 1996, respectively. The results of operations for the year ended December 31, 1998 were generally in line with management's expectations, except as described below.

Revenues

The Company's distribution partners commenced commercial sales of PHOTOFRIN in the Netherlands, Japan and Canada in 1995, in the United States in late 1996 and in France and Germany in late 1997. For the year ended December 31, 1998, the Company recorded royalty revenue of $2 million on end-user PHOTOFRIN sales of approximately $8.78 million. The 69% increase in royalty revenue relates primarily to PHOTOFRIN sales growth in the United States and to a lessor extent given the smaller sales base, incremental European sales compared to the same period in 1997. Looking forward to 1999, the Company expects PHOTOFRIN royalties to increase significantly with the U.S. launch of PHOTOFRIN as a palliative treatment for advanced lung cancer further contributing to a steady increase in sales volume.

During 1998, the Company received U.S. Food and Drug Administration (FDA) approval for two additional PHOTOFRIN indications. In January, the FDA approved the Company's application to expand the approval of PHOTOFRIN to include the treatment of early-stage lung cancer. In late December, the FDA granted approval for the treatment of advanced lung cancer with PHOTOFRIN. The Company's U.S. marketing partner, Sanofi Pharmaceuticals, Inc. (Sanofi), launched PHOTOFRIN as a palliative treatment for advanced lung cancer at the January 1999 Society of Thoracic Surgeons Conference.

Early in January 1999, the Company received notification that the health authorities in the United Kingdom had granted marketing clearance to PHOTOFRIN for the palliative treatment of both advanced esophageal and lung cancers.

The level of PHOTOFRIN sales may be affected during 1999 and thereafter by uncertainty of the price reimbursement structure for PHOTOFRIN in various jurisdictions; the ability to expedite product launches for PHOTOFRIN in Europe following receipt of additional regulatory approvals; sufficient product supply being available and the placement of additional medical lasers in key jurisdictions.

The extent of cash flow provided to the Company from PHOTOFRIN sales is dependent upon the marketing performance of Sanofi, Beaufour Ipsen, Wyeth Lederle Japan, Ltd. (Wyeth Lederle), and

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Kenneth Galbraith C.A.
Senior Vice President and Chief Financial Officer

The following information should be read in conjunction with the Company's 1998 consolidated financial statements and related notes included therein, which are prepared in accordance with generally accepted accounting principles in Canada (Canadian GAAP). These principles differ in certain respects from generally accepted accounting principles in the United States (U.S. GAAP). The differences as they effect the financial statements of the Company are described in Note 11 to the Company's audited 1998 consolidated financial statements. All amounts following are expressed in Canadian Dollars unless otherwise indicated.

Overview

Since its inception in 1981, the Company has been engaged primarily in the research and development of proprietary pharmaceut the commercial sale of suc expects to incur additional research and development, initial marketing approvals and significant revenues r

The Company has in commercialization of Visu incurred annual operating profitability will be depend the Company had an accu

Results of Operations

For the year ended Decemb common share. These resu $4.7 million, or $0.19 per c The results of operations fo expectations, except as d

Revenues

The Company's distributio Japan and Canada in 1995 For the year ended Decemb PHOTOFRIN sales of approx to PHOTOFRIN sales growt incremental European sales expects PHOTOFRIN royalti treatment for advanced lu

Kenneth Galbraith C.A.
Senior Vice President and Chief Financial Officer

In addition to overseeing QLT's financial operations, Mr. Galbraith's responsibilities extend to business development, human resources, information technology, technical operations and product manufacturing.

Mr. Galbraith has been instrumental in raising $250 million of equity capital used to fund the company's innovative and expanding development programs. He has also played a key role in the negotiation of seven strategic partnerships. In 1998, under his management, the manufacturing group completed the process development work for Visudyne™, reaching both target capacity and cost of goods.

"Our financial management strategy has always focused on maintaining a strong balance sheet with sufficient cash to fund promising long-term R&D activities, while aggressively pursuing other opportunities. We strive to ensure that our burn rate maximizes development in view of QLT's existing and projected cash resources. Last summer, we felt it was strategically important to strengthen our balance sheet in preparation for the commercialization of Visudyne™ therapy. Our success demonstrates the continued access to equity capital QLT has enjoyed, even in challenging markets."

"Beyond 1999, we look forward to managing the balance between top-line revenues generated from Visudyne™ sales and continued expenditures in our exciting R&D pipeline."

During 1998, the Company received U.S. Food and Drug Administration (FDA) approval for two additional PHOTOFRIN indications. In January, the FDA approved the Company's application to expand the approval of PHOTOFRIN to include the treatment of early-stage lung cancer. In late December, the FDA granted approval for the treatment of advanced lung cancer with PHOTOFRIN. The Company's U.S. marketing partner, Sanofi Pharmaceuticals, Inc. (Sanofi), launched PHOTOFRIN as a palliative treatment for advanced lung cancer at the January 1999 Society of Thoracic Surgeons Conference.

Early in January 1999, the Company received notification that the health authorities in the United Kingdom had granted marketing clearance to PHOTOFRIN for the palliative treatment of both advanced esophageal and lung cancers.

The level of PHOTOFRIN sales may be affected during 1999 and thereafter by uncertainty of the price reimbursement structure for PHOTOFRIN in various jurisdictions; the ability to expedite product launches for PHOTOFRIN in Europe following receipt of additional regulatory approvals; sufficient product supply being available and the placement of additional medical lasers in key jurisdictions.

The extent of cash flow provided to the Company from PHOTOFRIN sales is dependent upon the marketing performance of Sanofi, Beaufour Ipsen, Wyeth Lederle Japan, Ltd. (Wyeth Lederle), and Ligand Pharmaceuticals Inc. (Ligand). Under the Company's agreements with its marketing partners except Wyeth Lederle, the Company is entitled to a royalty on PHOTOFRIN product sales and/or a transfer price computed as a reimbursement of manufacturing costs. Under the terms of the Company's agreement with Wyeth Lederle, Wyeth Lederle has responsibility for final decisions related to the marketing and sale of PHOTOFRIN in Japan, including a determination of the appropriate level of marketing effort. The Company will receive between 26% and 29.5% of product sales of PHOTOFRIN in Japan. Wyeth Lederle is responsible for marketing and distribution costs and manufacturing costs. The Company is responsible for payment of all third party royalties.

The Company did not receive any licensing fees or milestone payments during 1998. In 1997, the Company received milestone payments of $2.8 million (U.S.$2 million) from Beaufour Ipsen relating to the commercial launch of PHOTOFRIN in France and the regulatory approval of PHOTOFRIN in Germany. In 1996, the Company earned and recorded revenue from collaborative arrangements totaling $9.5 million (U.S.$7 million), including a $2.7 million (U.S.$2 million) access fee from Beaufour Ipsen which was paid in 1996 and a $6.8 million (U.S.$5 million) access fee from Sanofi which was paid in 1997.

The Company expects to receive licensing fees and milestone payments in the future from existing and new collaborative arrangements. The extent and timing of such additional licensing fees and milestone payments, if any, will be dependent upon the overall structure of current and proposed agreements, including the distribution of profits from product sales.

Interest and other income for the year ended December 31, 1998 decreased by 13% compared to 1997. During the fourth quarter of 1997, significant foreign exchange gains were recorded. Excluding the effect of net foreign exchange gains, interest and other income increased 7% from 1997 reflecting higher interest yields during 1998. Interest and other income for the year ended December 31, 1997 increased by 91% compared to levels in 1996 due primarily to higher average cash balances, offset partially by lower interest yields, and foreign exchange gains on the Company's foreign currency denominated cash balances. The Company expects that interest and other income will continue to fluctuate in relation to cash balances, interest yields and foreign exchange rates. See "Liquidity and Capital Resources".

Costs and Expenses

Total costs and expenses, excluding amortization, for the year ended December 31, 1998 increased by 22% from 1997. Total costs and expenses, excluding amortization, for the year ended December 31, 1997 increased by 53% compared to 1996.

Research and Development Costs

Research and development costs increased by 24% in 1998 compared to 1997. The Company originally expected that research and development costs would be approximately 35% greater than 1997, however certain activities were deferred to future periods. The increase in 1998 relates primarily to increased personnel; the increased scale of manufacturing, formulation development, and validation activities for verteporfin; significant incremental costs associated with the ongoing Visudyne™ Phase III age-related macular degeneration (AMD) and PHOTOFRIN Phase IV esophageal cancer clinical trials, and; the initiation of the Visudyne™ AMD Phase IIIb and PHOTOFRIN Barrett's esophagus Phase III clinical trials. Research and development costs for 1997 were 67% higher than 1996 for similar reasons.

On February 6, 1995, the Company signed an agreement with CIBA Vision Ophthalmics AG (CIBA Vision) to pursue worldwide joint development of verteporfin as a potential treatment for certain eye diseases. Under the terms of that agreement, the Company is responsible for 40% of research and development costs for verteporfin and CIBA Vision is responsible for the remaining 60%. Revenues realized from product sales of Visudyne™ for treatment of age related macular degeneration or other eye diseases will be shared on an equal basis by the Company and CIBA Vision after deductions for marketing costs, manufacturing costs and third party royalties.

Under the Company's agreement with Beaufour Ipsen, which commenced in 1997, Beaufour Ipsen will fund research and development efforts for oncology in Europe up to U.S.$15 million. As of December 31, 1998, the Company has received or earned U.S.$2.6 million ($3.9 million) of funding. Aggregate costs in excess of U.S.$15 million, will be shared on an equal basis by the Company and Beaufour Ipsen.

The Company and its co-development partners reconcile joint development costs, on a quarterly basis, which has typically resulted in ongoing funding payments to the Company. The Company records such amounts as a reduction to research and development costs.

On April 30, 1998, the Company announced the formation of a strategic alliance with C.R. Bard (Bard) to develop a therapeutic system and procedure for the reduction of arterial restenosis utilizing localized delivery of photodynamic therapy (QLT-Bard Alliance). Under the terms of the partnership, Bard will fund product development and clinical research and market the final products on an exclusive worldwide basis. QLT is entitled to receive royalty payments from Bard and has retained an option to co-fund research and development at a later date in exchange for an increased share of sales revenue. This agreement has not had a material effect on research and development costs for 1998 nor is it expected to in 1999.

On September 30, 1998, Bard finalized an agreement to sell certain of its businesses, products and technologies that comprise its coronary catheter laboratory business to Arterial Vascular Engineering, Inc. (AVE) for U.S.$600 million (Bard-AVE Transaction). Under the terms of the Company's agreement with Bard, Bard has the right to assign its rights and obligations under the agreement in connection with the sale of all or a substantial portion of Bard's cardiology related assets. Although pre-clinical work is being carried out by AVE, as of the date of this report, the Company has not received formal written notification by Bard that it has exercised its rights of assignment under the QLT-Bard Alliance in connection with the Bard-AVE Transaction.

The Company expects to continue incurring substantial additional research and development expenses in the future, due to expansion of research and development programs; potential technology in-licensing and regulatory-related expenses; preclinical and clinical testing of the Company's various products under development; and production scale-up and manufacturing of products used in clinical trials. The Company believes that research and development costs for 1999 will be approximately 20% greater than for the 1998 fiscal year.

Selling, General and Administrative Expenses

Total selling, general and administrative expenses for the year ended December 31, 1998 were 15% higher compared to 1997. Contributing factors were, in descending order: a significant increase in third party royalty payments commensurate with the increase in royalty revenues; an increase in commercial operations activities, including costs related to obtaining the European CE mark for the Company's fiber optic device product (OPTIGUIDE™) and additional support personnel; and higher personnel recruitment costs. The Company originally expected total selling, general and administrative expenses would be approximately 5% greater than for the 1997 fiscal year. Total selling, general and administrative expenses for 1997 were 17% higher than in 1996. The increase related primarily to increased personnel and associated hiring costs; costs of increased corporate development activities relating to the formation of new strategic alliances; and pre-marketing activities for PHOTOFRIN. The Company believes that selling, general and administrative expenses for 1999 will be approximately 20% greater than for the 1998 fiscal year.

Amortization

Amortization expense relates to the amortization of property and equipment, patents, licenses and rights. For the year ended December 31, 1998 amortization expense was 43% lower than the amount recorded in 1997 due to certain rights being fully amortized late in 1997. Compared to 1996, 1997 amortization expense was 14% higher due to a higher level of capital additions during the year and the incremental amortization impact of significant additions in late 1996. The Company believes that amortization expense for 1999 will be approximately 35% greater than for the 1998 fiscal year.

Effect of Inflation

The Company does not believe that inflation has a significant effect on its business.

Implications of Year 2000 Issue

The Year 2000 Issue generally refers to the business implications of the arrival of the new millennium on computer hardware systems and software. On January 1, 2000 many computer systems could either fail completely or create erroneous data as a result of misinterpretation of the year. The results of such failures could range from relatively minor processing inaccuracies to catastrophic system malfunctions.

The Company has formed a Year 2000 Project Steering Committee and appointed a dedicated Project Coordinator to address the Year 2000 Issue as it relates to the Company. An initial assessment of both information technology (IT) and non-IT systems has been completed and an action plan has been prepared to address identified critical internal information systems weaknesses prior to September 30, 1999, which is prior to the likely occurrence of any Year 2000 issues. The Company does not believe that it is at significant risk relating to the Year 2000 Issue given the following factors: the general simplicity of internal systems and the nature of the Company's operations; most software and hardware currently in use is less than two years old of which their purchase was subject to Year 2000 compliance representations; most software in use is readily available "off the shelf" third party, brand name products; and non-compliant critical systems identified will be upgraded, converted or replaced.

However, the Company does conduct a significant portion of its activities with third parties, including suppliers, manufacturers and distributors. The Company has initiated formal communications with significant third parties to determine the extent to which the Company's interface systems are vulnerable to the failure of those third parties to remediate their own Year 2000 Issues and ensure that such third parties will be Year 2000 compliant prior to January 1, 2000. There is no guarantee that the systems of other companies upon which the Company's systems rely will be remediated or compliant on a timely basis and will not have an adverse impact on the Company's business. The most reasonably likely worst case scenarios would include corruption of data contained in the Company's internal information systems, hardware failure, and the failure of infrastructure services provided by government agencies and other third parties. A contingency plan encompassing all critical systems will be developed, implemented and tested by September 30, 1999 with an emphasis on off-site manufacturing and inventory storage. The Company anticipates its contingency plan to include, among other things, manual "work-arounds" for software and hardware failures, as well as substitution of critical systems, if necessary.

The Company believes that the cost of addressing the Year 2000 Issue will not have a material effect on the results of operations or financial condition of the Company. Total costs associated with the company's Year 2000 Project is estimated to be less than $200,000, with approximately 50% expended to date. Any costs incurred relating to the Year 2000 Issue will be expensed as incurred and funded by working capital.

Liquidity and Capital Resources

Since inception the Company has financed product development, operations and capital expenditures primarily from public and private sales of equity securities, licensing and funding arrangements with strategic partners and interest income.

At December, 31, 1998, the Company had $78.2 million of available cash resources, comprised of cash, cash equivalents and investment securities, 99% of which was invested in liquid, investment-grade securities. In aggregate, cash, cash equivalents, and short-term and long-term investment securities decreased by approximately $11.6 million during the year ended December 31, 1998. The decrease relates to the net effect of the Company's annual operating loss net of amortization ($22.9 million), working capital change ($6 million) and property and equipment capital expenditures ($7 million) offset by the net proceeds ($21.9 million) of a share offering of one million common shares at $23.00 per share on July 24, 1998 and less significantly by the aggregate proceeds received from the exercise of employees' stock options by employees and directors ($2.4 million) during the year. Since year end and up to February 23, 1999, the Company's available cash resources has been strengthened further with an additional $18.8 million of proceeds from the exercise of common share stock options and warrants.

Dr. Mohammad Azab, M.D.
Vice President, Clinical Research and Medical Affairs

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Dr. Mohammad Azab, M.D.
Vice President, Clinical Research and Medical Affairs

Dr. Mohammad Azab joined QLT in early 1997 after five years at Zeneca Pharmaceuticals, where he managed the firm's clinical drug development programs in oncology and gynecology. Under his experienced leadership, QLT's clinical department has more than doubled to 40 people, and now includes expertise in pharmacokinetics, data management, statistics and medical writing.

"We bolstered our team to meet the challenges of running three major Phase III programs simultaneously – two in ophthalmology and one in oncology. By expanding our data management group and adding skilled people in clinical quality control and GCP compliance, we're now equipped to perform complex data analysis very quickly – as shown by the rapid turnaround of the positive initial results from our AMD trial."

"The TAP studies, which are being conducted entirely in-house and without the use of contract research organizations, have been widely praised for their high quality by the ophthalmology community. These trials are a perfect example of what our clinical team is capable of doing. We're eager and ready to play a key role as QLT continues to aggressively expand its development pipeline."

Liquidity and Capital Resources

Since inception the Company has financed product development, operations and capital expenditures primarily from public and private sales of equity securities, licensing and funding arrangements with strategic partners and interest income.

At December, 31, 1998, the Company had $78.2 million of available cash resources, comprised of cash, cash equivalents and investment securities, 99% of which was invested in liquid, investment-grade securities. In aggregate, cash, cash equivalents, and short-term and long-term investment securities decreased by approximately $11.6 million during the year ended December 31, 1998. The decrease relates to the net effect of the Company's annual operating loss net of amortization ($22.9 million), working capital change ($6 million) and property and equipment capital expenditures ($7 million) offset by the net proceeds ($21.9 million) of a share offering of one million common shares at $23.00 per share on July 24, 1998 and less significantly by the aggregate proceeds received from the exercise of employees' stock options by employees and directors ($2.4 million) during the year. Since year end and up to February 23, 1999, the Company's available cash resources has been strengthened further with an additional $18.8 million of proceeds from the exercise of common share stock options and warrants.

The Company is exposed to market risk related to changes in interest and foreign currency exchange rates, each of which could adversely affect the value of the Company's current assets and liabilities. At the end of the year, the Company had an investment portfolio consisting of interest bearing securities with an average maturity of less than ninety days. The interest bearing securities are subject to interest rate risk and will fall in value if market interest rates increase. If market interest rates were to increase immediately and uniformly by 10% from levels at December 31, 1998, the fair value of the portfolio would decline by an immaterial amount. Being the Company has the ability to hold its fixed income investments until maturity, it does not expect its operating results or cash flows to be affected to any significant degree by a sudden change in market interest rates relative to its investment portfolio. The Company has not entered into any forward currency contracts or other financial derivatives to hedge foreign exchange risk. Therefore, the Company is subject to foreign currency transaction and translation gains and losses. The Company does not believe a sudden or significant change in foreign exchange rates would have a material effect on future operating results or cash flows.

The approval of PHOTOFRIN in Canada on April 20, 1993 triggered certain additional payments to several unrelated third parties with respect to the Company's acquisition of the rights to PHOTOFRIN in 1987. On June 19, 1993, the Company issued 231,589 common shares with a market value of U.S.$2 million to a group of former licensees of PHOTOFRIN as a component of the acquisition cost. This issuance of common shares reduced non-current liabilities by $2,532,500 (U.S.$2 million), being the obligation originally recorded in 1987. In addition, the Company made a payment to Johnson & Johnson of U.S.$250,000 on April 19, 1994 and made a further payment of U.S.$500,000 on April 19, 1995. Additional payments to Johnson & Johnson commenced on April 19, 1996 and will be required annually thereafter based on the level of PHOTOFRIN sales, but in no event will annual payments exceed U.S.$500,000 nor will cumulative payments exceed U.S.$4.2 million. Subsequently, payments of U.S.$18,418, U.S.$124,505 and U.S.$235,080, related to the annual periods ended April 19, 1996, 1997 and 1998, respectively, have been made to Johnson & Johnson.

Aside from the Company's obligation to Johnson & Johnson and the new facility construction contract identified below, the Company had no material long-term obligations as of December 31, 1998.

During the third quarter of 1998, the Company completed an acquisition of land located in Vancouver, B.C. for the site of its new office and research facility. Construction commenced during the final quarter of the year and estimated completion and occupancy of the new facility is expected during December, 1999. Total project cost, including land and capitalized financing and other soft costs, is expected to be approximately $22 million. As at December 31, 1998, $4.1 million had been expended or incurred on this project. The Company has entered into a fixed price construction contract for the base building in the amount of $16.1 million, of which $0.7 million for the first progress claim was accrued at year-end. The Company has secured a commitment from a major Canadian financial institution to provide up to $15.6 million of interim construction financing, which upon the completion of construction would be replaced by a fixed rate term loan of $14 million.

The Company believes capital expenditures for 1999 will be significantly higher due to the construction of its new facility. Excluding the effect of new facility project costs for 1999 and from 1998 figures, capital expenditures should not be significantly different from the level of capital spending in 1998.

The Company believes that its available cash resources and working capital should be sufficient to satisfy the cash requirements of product development programs and the repayment of obligations to Johnson & Johnson, for approximately the next three years. The Company expects to continue to receive cash flow from its share of the product sales of PHOTOFRIN in 1999 and beyond based on continued marketing efforts in the United States, certain countries in Europe, Japan and Canada. The Company expects to receive royalty revenue in the future from other jurisdictions if regulatory and pricing approvals are received and, where appropriate, as marketing and distribution arrangements are established in each jurisdiction to allow commercial launches of PHOTOFRIN. In addition, the Company expects to receive an equal share of profits from its joint profit sharing arrangement with CIBA Vision for Visudyne™ once the appropriate regulatory submissions are filed and approved and the product has been launched. Depending on the overall structure of current and future strategic alliances, the Company may have additional capital requirements related to the further development, marketing and distribution of PHOTOFRIN and Visudyne™.

The Company's working capital and capital requirements will depend upon numerous factors, including: the progress of the Company's preclinical and clinical testing; fluctuating or increasing manufacturing requirements and research and development programs; timing and cost of obtaining regulatory approvals; levels of resources that the Company devotes to the development of manufacturing, marketing and support capabilities; technological advances; status of competitors; cost of filing, prosecuting and enforcing the Company's patent claims and other intellectual property rights; and the ability of the Company to establish collaborative arrangements with other organizations.

The Company expects that it may require additional capital in the future to fund clinical and product development costs for certain photodynamic therapy product applications, including the costs associated with conducting clinical trials of Visudyne™ for the treatment of other ophthalmic indications. Accordingly, the Company anticipates funding research and development activities from a combination of sources, including product licensing, joint development and other financing arrangements. In addition, the Company may issue debt or equity securities in the future if it determines that additional cash resources could be obtained under favourable financial market conditions, or if future development funding requirements cannot be satisfied with available cash resources. No assurance can be given that additional funding will be available or, if available, on terms acceptable to the Company. If adequate capital is unavailable, the Company may have to substantially reduce or eliminate expenditures for research, development, clinical testing, manufacturing and marketing for certain photodynamic therapy applications.

Management Report

The consolidated financial statements contained in this annual report have been prepared by management in accordance with generally accepted accounting principles and have been approved by the Board of Directors. The integrity and objectivity of these consolidated financial statements are the responsibility of management. In addition, management is responsible for all other information in the annual report and for ensuring that this information is consistent, where appropriate, with the information contained in the consolidated financial statements.

In support of this responsibility, management maintains a system of internal controls to provide reasonable assurance as to the reliability of financial information and the safeguarding of assets. The consolidated financial statements may include amounts which are based on the best estimates and judgements of management.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control and exercises this responsibility principally through the Audit Committee. The Audit Committee consists of three independent directors not involved in the daily operations of the Company. The functions of the Audit Committee are to review the quarterly and annual consolidated financial statements, review the adequacy of the system of internal controls, review any relevant accounting, financial and security regulatory matters and recommend the appointment of external auditors. The Audit Committee meets on a quarterly basis with management and the external auditors of the Company to satisfy itself that their responsibilities have been properly discharged.

The external auditors, Deloitte & Touche LLP, conduct an independent examination, in accordance with generally accepted auditing standards, and express their opinion on the consolidated financial statements. Their examination includes a review of the Company's system of internal controls and appropriate tests and procedures to provide reasonable assurance that the consolidated financial statements are, in all material respects, presented fairly and in accordance with generally accepted accounting principles in Canada. The external auditors have free and full access to the Audit Committee with respect to their findings concerning the fairness of financial reporting and the adequacy of internal controls.

JULIA G. LEVY, Ph.D.
President and Chief Executive Officer

KENNETH H. GALBRAITH, C.A.
Senior Vice President and Chief Financial Officer

Auditors' Report

To the Shareholders of QLT PhotoTherapeutics Inc.

We have audited the consolidated balance sheets of QLT PhotoTherapeutics Inc. as at December 31, 1998 and 1997 and the consolidated statements of operations, cash flows and changes in shareholders' equity for each of the years in the three year period ended December 31, 1998. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the company as at December 31, 1998 and 1997 and the results of its operations, cash flows and changes in shareholders' equity for each of the years in the three year period ended December 31, 1998 in accordance with accounting principles generally accepted in Canada consistently applied.

Deloitte & Touche

DELOITTE & TOUCHE LLP
Chartered Accountants
Vancouver, Canada
February 12, 1999
(Except for Note 13(a) for which the date is February 23, 1999)

Consolidated Balance Sheets

As at December 31, (In thousands of Canadian Dollars)	1998	1997
ASSETS		
Current assets		
Cash and cash equivalents	$ 74,275	$ 60,217
Short-term investment securities	3,970	26,684
Accounts receivable (Note 2)	7,102	4,134
Inventories (Note 3)	6,555	2,708
Other current assets	1,395	426
	93,297	94,169
Long-term investment securities	—	2,887
Property and equipment (Note 4)	9,626	3,768
Intangible assets (Note 5)	300	399
	$ 103,223	$ 101,223
LIABILITIES		
Current liabilities		
Accounts payable	$ 5,807	$ 4,390
Accrued liabilities	2,338	1,985
	8,145	6,375
SHAREHOLDERS' EQUITY		
Share capital (Note 6)		
Authorized		
100,000,000 common shares without par value		
5,000,000 first preference shares without par value, issuable in series		
Issued and outstanding		
Common shares		
December 31, 1998 – 27,263,652		
December 31, 1997 – 26,101,762	228,953	204,652
First preference shares, series D		
December 31, 1998 – 368,069		
December 31, 1997 – 368,069	6,850	6,850
Accumulated deficit	(140,725)	(116,654)
	95,078	94,848
	$ 103,223	$ 101,223

COMMITMENTS (Note 10)

See accompanying notes to the consolidated financial statements.

Approved by the Board:

E.D. SCOTT
Director

J. G. LEVY
Director

Consolidated Statements of Operations

Year ended December 31, (In thousands of Canadian Dollars except per share information)	1998	1997	1996
Revenues			
Royalties on product sales	$ 2,004	$ 1,183	$ 669
Revenue from collaborative arrangements (Note 7)	—	2,790	9,500
Interest and other income	5,571	6,368	3,328
	7,575	10,341	13,497
Costs and expenses			
Research and development	23,890	19,214	11,480
Selling, general and administrative	6,544	5,688	4,847
Amortization	1,212	2,122	1,867
	31,646	27,024	18,194
Net loss	$ (24,071)	$ (16,683)	$ (4,697)
Net loss per common share	$ (0.90)	$ (0.64)	$ (0.19)
Weighted average number of common shares outstanding	26,637	26,036	24,473

See accompanying notes to the consolidated financial statements.

Consolidated Statements of Cash Flows

Year ended December 31, (In thousands of Canadian Dollars)	1998	1997	1996
Cash provided by (used in) operating activities			
Net loss for the year	$ (24,071)	$ (16,683)	$ (4,697)
		2,122	1,867
		4,754	(8,268)
		(1,463)	(269)
		115	(139)
		2,344	993
		693	861
		(8,118)	(9,652)
		27,280	(53,565)
		(2,887)	4,295
		(1,919)	(1,616)
		22,474	(50,886)
		2,674	85,511
		—	6,850
		2,674	92,361
		17,030	31,823
		43,187	11,364
		$ 60,217	$ 43,187

sion of 500,000 Series "C" First

Alexandra Mancini
Vice President, Regulatory Affairs

Year ended December 31, (In tho

Revenues

Royalties on product sales

Revenue from collaborative

Interest and other income

Costs and expenses

Research and development

Selling, general and admini

Amortization

Net loss

Net loss per common share

Weighted average number of

See accompanying notes to the c

Alexandra Mancini
Vice President, Regulatory Affairs

Ms. Mancini joined QLT in 1992 after a decade in the pharmaceutical and food industries, most recently at Parke-Davis Pharmaceutical Research in Ann Arbor, Michigan. Her contributions to QLT have been significant.

Ms. Mancini led the compilation of data from clinical trials conducted in the late 1980s by a former QLT partner. She then prepared the submission that resulted in a number of international regulatory approvals for PHOTOFRIN. This achievement is made all the more significant by the fact that these approvals mark the first ever for photodynamic therapy – a new technology involving a drug-device combination.

1998 was a banner year for Ms. Mancini and her team, having received two FDA approvals for PHOTOFRIN. The first, which was an approval for early stage lung cancer, represented a landmark decision since it was the first time the technology was approved as a "curative" treatment in North America. The second approval, which followed a unanimous recommendation by the FDA advisory committee in September, was for the palliative treatment of advanced lung cancer.

"The Visudyne™ filing will require months of intense effort in 1999 as we continue to work on additional PHOTOFRIN approvals in Europe and Canada. Our determination to get the job done however, comes from knowing the number of lives that will be improved by the availability of our products."

Consolidated Statements of Cash Flows

Year ended December 31, (In thousands of Canadian Dollars)	1998	1997	1996
Cash provided by (used in) operating activities			
Net loss for the year	$ (24,071)	$ (16,683)	$ (4,697)
Items not involving a current cash flow			
Amortization	1,212	2,122	1,867
Changes in non-cash working capital components			
Accounts receivable	(2,968)	4,754	(8,268)
Inventories	(3,847)	(1,463)	(269)
Other current assets	(969)	115	(139)
Accounts payable	1,417	2,344	993
Accrued liabilities	353	693	861
	(28,873)	(8,118)	(9,652)
Cash provided by (used in) investing activities			
Short-term investment securities	22,714	27,280	(53,565)
Long-term investment securities	2,887	(2,887)	4,295
Purchase of property and equipment	(6,971)	(1,919)	(1,616)
	18,630	22,474	(50,886)
Cash provided by (used in) financing activities			
Issuance of common shares	24,301	2,674	85,511
Issuance of Series "D" First Preference Shares	—	—	6,850
	24,301	2,674	92,361
Net increase in cash and cash equivalents	14,058	17,030	31,823
Cash and cash equivalents, beginning of year	60,217	43,187	11,364
Cash and cash equivalents, end of year	$ 74,275	$ 60,217	$ 43,187

Supplemental Disclosure of Non-Cash Financing Activities

During the year ended December 31, 1996, the Company issued 1,180,453 common shares upon the conversion of 500,000 Series "C" First Preference Shares including accrued unpaid cumulative dividends of $1,365,483.

See accompanying notes to the consolidated financial statements.

Consolidated Statements of Changes in Shareholders' Equity

Year ended December 31, (In thousands of Canadian Dollars except per share information)	Common Shares		Preference Shares		Accumulated Deficit	Total Shareholders' Equity
	Shares	Amount	Shares	Amount		
Balance at January 1, 1996	19,996,339	$ 109,202	500,000	$ 5,900	$ (93,908)	$ 21,194
Exercise of stock options at prices ranging from $5.50 to $24.00 per share	1,092,400	10,606	—	—	—	10,606
Issuance of common shares at $21.25 per share, net of issuance costs of $5,158	3,450,000	68,154	—	—	—	68,154
Conversion of Series "C" First Preference Shares to common shares at par value plus accrued unpaid cumulative dividends	1,180,453	7,266	(500,000)	(5,900)	(1,366)	—
Issuance of Series "D" First Preference Shares to Sanofi Pharmaceuticals, Inc.	—	—	368,069	6,850	—	6,850
Issuance of common shares to Beaufour Ipsen at $34.11 per share	197,863	6,750	—	—	—	6,750
Net loss	—	—	—	—	(4,697)	(4,697)
Balance at December 31, 1996	25,917,055	201,978	368,069	6,850	(99,971)	108,857
Exercise of stock options at prices ranging from $5.88 to $31.85 per share	184,707	2,674	—	—	—	2,674
Net loss	—	—	—	—	(16,683)	(16,683)
Balance at December 31, 1997	26,101,762	$ 204,652	368,069	$ 6,850	$(116,654)	$ 94,848
Exercise of stock options at prices ranging from $9.00 to $21.75 per share	161,890	2,446	—	—	—	2,446
Issuance of common shares at $23.00 per share, net of issuance costs of $1,145	1,000,000	21,855	—	—	—	21,855
Net loss	—	—	—	—	(24,071)	(24,071)
Balance at December 31, 1998	27,263,652	$ 228,953	368,069	$ 6,850	$(140,725)	$ 95,078

See accompanying notes to the consolidated financial statements.

The Company is a biopharmaceutical corporation engaged in the research, development and commercialization of light-activated drugs used in photodynamic therapy.

Note 1.
Significant
Accounting Policies

The consolidated financial statements have been prepared in accordance with generally accepted accounting principles in Canada (Canadian GAAP). These principles differ in certain respects from generally accepted accounting principles in the United States (U.S. GAAP). The differences as they effect the financial statements of the Company are described in Note 11. All amounts are expressed in Canadian Dollars unless otherwise indicated.

Principles of Consolidation

These consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany transactions have been eliminated.

Use of Estimates

Preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting periods presented. Actual results could differ from estimates made by management.

Foreign Currency Translation

Monetary assets and liabilities are translated into Canadian dollars at the exchange rate in effect at the balance sheet date and non-monetary assets and liabilities are translated at rates of exchange in effect when the assets were acquired or obligations incurred. Revenues and expenses are translated at exchange rates in effect at the time of the transactions. Foreign exchange gains and losses are included in other income.

Segmented Information

The Company is considered to operate in one industry segment and currently generates royalty revenue from a single pharmaceutical product. Substantially all royalty revenue is attributable to product sales outside of Canada for all periods presented, with the majority in the United States.

Cash and Cash Equivalents

Cash equivalents include highly liquid investments with original maturities of ninety days or less at the date of purchase and are valued at cost plus accrued interest which approximates fair value.

Note 1.
Significant
Accounting Policies (continued)

Investment Securities

Short-term investment securities consist principally of investment grade commercial paper (R1-M or higher), bankers' acceptances or certificates of deposit with varying maturities of between ninety days and one year at the date of purchase. Long-term investment securities consist of government bonds with maturities in excess of one year at the date of purchase. All investment securities are valued at cost plus accrued interest which approximates fair value.

Inventories

Raw materials inventory is valued at the lower of cost and replacement cost. Finished goods and work in process inventories are valued at the lower of cost and net realizable value. Cost is determined using weighted average cost.

Property and Equipment

Property and equipment are recorded at cost and amortized on a declining-balance basis at 20% per annum, except for leasehold improvements which are amortized on a straight-line basis over the shorter of their estimated useful lives or lease term. The Company assesses potential impairment of research equipment by determining the extent of continued productive use of the equipment in the conduct of research and development. The Company makes reviews for the impairment of other long lived assets whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. An impairment loss would be recognized when estimates of future cash flows expected to result from the use of an asset and its eventual disposition are less than its carrying amount. No such impairment losses have been identified by the Company for the years ended December 31, 1998 and 1997.

Intangible Assets

Intangible assets consist of: (i) the cost of acquiring patents, licenses and rights to PHOTOFRIN which is being amortized over a ten year period; and (ii) the cost of acquiring certain marketing rights for PHOTOFRIN which is being amortized over five years. The costs of servicing the Company's patents and other intellectual property are expensed as incurred. The Company assesses potential impairment of the intangible assets by measuring the expected net recovery from products based on these rights on an annual basis.

Revenue Recognition

Royalties on product sales are recognized as earned under the Company's marketing and distribution agreements which generally are consistent with the period of the product sale by the distributors. Revenue from collaborative arrangements is recognized as income in the period earned in accordance with the terms of the related agreement.

Research and Development

Research and development costs are expensed in the period incurred, net of amounts reimbursed by third parties in accordance with collaborative arrangements.

Net Loss Per Common Share

Net loss per common share, or basic loss per share, is computed using the weighted average number of common shares outstanding during the period. Fully-diluted loss per common share has not been disclosed as the effect of common shares issuable upon the exercise of options or warrants would be anti-dilutive.

Note 2.

Accounts Receivable

(In thousands)	1998	1997
Reimbursable co-development costs	$ 5,408	$ 1,817
Royalties, trade and other	1,694	2,317
	$ 7,102	$ 4,134

	1998	1997
	$ 578	$ 1,672
	4,262	—
	1,715	1,036
	$ 6,555	$ 2,708

	1998 Net Book Value	1997 Net Book Value
	$ 201	$ 378
	2,078	1,685
	2,109	1,705
	1,156	—
	1,773	—
	2,309	—
	$ 9,626	$ 3,768

da except for $1,782,000
190,000 (1997 – $536,000)

Dr. Edwin Levy, Ph.D
Vice President, Corporate Development

Note 1.
Significant
Accounting Policies (continued)

Investment Securities

Short-term investment securities consist principally of investment grade commercial paper (R1-M or higher), bankers' acceptances or certificates of deposit with varying maturities of between ninety days and one year at the date of purchase. Long-term investment securities consist of government bonds with maturities in excess of one year at the date of purchase. All investment securities are valued at cost plus accrued interest which approximates fair value.

Inventories

Raw materials inventory is valued at the lower of cost and replacement cost. Finished goods and work in process inventories are valued at the lower of cost and net realizable value. Cost is determined using weighted average cost.

Property and Equipment

Property and equipment are recorded at cost and amortized on a declining-balance basis at 20% per annum, except for leasehold improvements
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Intangible Assets

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Revenue Recognition

Royalties on product sales
which generally are consist
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Research and Development

Research and development
in accordance with collabo

Net Loss Per Common Share

Net loss per common share
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common shares issuable up

Dr. Edwin Levy, Ph.D
Vice President,
Corporate Development

Dr. Ed Levy is primarily responsible for the formation and management of QLT's strategic alliances including CIBA Vision, Sanofi Pharmaceuticals, and Arterial Vascular Engineering. In addition, Dr. Levy manages QLT's device group and oversees intellectual property issues regarding QLT's portfolio of patents.

Under his tenure, the device team – in conjunction with various laser partners – has developed innovative light sources for different applications of photodynamic therapy, including a 630nm diode laser for treating internal cancers, and a multi-head light-emitting diode laser for treating skin cancer.

"Our strategic alliances include partnerships to market and distribute our company's products, as well as working relationships with device companies. Effective guidance of our partnerships is achieved through joint management and operational committees."

"As we approach top-tier status, we will continue to look for new strategic partnerships and evaluate technologies complementary to our existing business units in order to sustain the growth expected from Visudyne™."

Note 2.
Accounts Receivable

(In thousands)	1998	1997
Reimbursable co-development costs	$ 5,408	$ 1,817
Royalties, trade and other	1,694	2,317
	$ 7,102	$ 4,134

Note 3.
Inventories

(In thousands)	1998	1997
Raw materials and supplies	$ 578	$ 1,672
Work-in-process	4,262	—
Finished goods	1,715	1,036
	$ 6,555	$ 2,708

Note 4.
Property and Equipment

(In thousands)			1998	1997
	Cost	Accumulated Amortization	Net Book Value	Net Book Value
Leasehold improvements	$ 1,160	$ (959)	$ 201	$ 378
Office furnishings, equipment and software	3,414	(1,336)	2,078	1,685
Research equipment	5,102	(2,993)	2,109	1,705
Commercial manufacturing equipment	1,156	—	1,156	—
Building under construction	1,773	—	1,773	—
Land	2,309	—	2,309	—
	$ 14,914	$ (5,288)	$ 9,626	$ 3,768

As at December 31, 1998, the Company's tangible assets were all located in Canada except for $1,782,000 (1997 – $696,000) of net commercial manufacturing and research equipment of which $1,490,000 (1997 – $536,000) is located in the United States and $292,000 (1997 – $160,000) in Europe and Japan.

Note 5.
Intangible Assets

(In thousands)	1998	1997
Patents, licenses and rights	$ 7,392	$ 7,392
Less: Accumulated amortization	(7,092)	(6,993)
	$ 300	$ 399

Patents, licenses and rights consist of (i) the rights, title and interest respecting the former photodynamic therapy business of Johnson & Johnson, including the rights to the light-activated drug, PHOTOFRIN, purchased by the Company in 1987 and (ii) certain European marketing rights acquired by the Company in 1996 from American Cyanamid Company (Cyanamid). Additional payments based on a percentage of worldwide sales between April 1995 and April 2013 are payable to Johnson & Johnson subject to an annual maximum of U.S.$500,000 and a cumulative maximum of U.S.$4,200,000. Such payments are recorded as selling expenses in the fiscal year relating to product sales. As of December 31, 1998, the Company has made cumulative payments to Johnson & Johnson of U.S.$378,003 pursuant to the acquisition of such rights.

Note 6.
Share Capital

(a) Authorized Shares

During the three year period ended December 31, 1998 there were no changes to the authorized share capital of the Company.

(b) Shareholder Protection Rights Plan

On March 17, 1992, the Company adopted a Shareholder Protection Rights Plan (the Plan) to protect its shareholders from unfair, abusive or coercive take-over strategies. The Plan was approved by the shareholders of the Company on April 28, 1992, subsequently amended by the Company on March 31, 1997 and re-confirmed by shareholders on May 12, 1997. The Plan, as amended, will remain in effect until March 17, 2002, unless terminated earlier. Under the Plan, as amended, holders of common shares are entitled to one share purchase right for each common share held. Generally, if any person or group makes a take-over bid, other than a bid permitted under the plan (a Permitted Bid) or acquires 20% or more of the Company's outstanding common shares without complying with the Plan, the Plan will entitle these holders of share purchase rights to purchase, in effect, common shares of the Company at 50% of the prevailing market price. A take-over bid for the Company can avoid the dilutive effects of the share purchase rights, and therefore become a Permitted Bid, if it complies with provisions of the Plan or if it is expressly approved by the Board of Directors.

(c) Stock Options

The Company has three incentive stock option plans which are identified below. All plans provide for the grant of options to purchase common shares to Directors, executive officers and employees of the Company, or any of its subsidiaries, to provide incentive to develop the growth of the Company. Under all plans, vesting of stock options generally occurs as follows: 1) for Directors – after a one year period, 2) for executive officers – equally over a three year period, 3) for senior employees – one half at time of grant and the remainder equally over three years, and 4) for other employees – immediately upon grant. Each plan also contains a provision which allows accelerated vesting for individual option holders under certain conditions.

(i) 1991 Incentive Stock Option Plan (1991 Plan) The 1991 Plan, which provides for the issuance of up to 1,500,000 common shares, was approved by shareholders in April 1992 and the maximum term of any option granted under the 1991 Plan is ten years. The 1991 Plan automatically terminated on May 17, 1996, but options granted before this date may be exercised until they expire in accordance with their original terms. At December 31, 1998, options to purchase an aggregate total of 83,836 common shares were outstanding under the 1991 Plan and exercisable at prices ranging between $8.75 and $11.13 per common share.

(ii) 1995 Incentive Stock Option Plan (1995 Plan) The 1995 Plan, which provides for the issuance of up to 2,000,000 common shares, was approved by shareholders in May 1995 and the maximum term of any option granted under the 1995 Plan is five years. The 1995 Plan automatically terminated on February 10, 1998, but options granted before this date may be exercised until they expire in accordance with their original terms. At December 31, 1998, options to purchase an aggregate total of 1,594,063 common shares were outstanding under the 1995 Plan and exercisable in the future at prices ranging between $9.00 and $34.25 per common share.

(iii) 1998 Incentive Stock Option Plan (1998 Plan) The 1998 Plan, which provides for the issuance of up to 2,500,000 common shares, was approved by shareholders in May 1998. The maximum term of any option granted under the 1998 Plan is five years. The exercise price of an option granted is set by the Executive Compensation Committee (Committee), of the Board of Directors, at the time of grant and may not be less than the fair market price of the common shares on the date of the grant. No option may be granted under the 1998 Plan if it would result in the optionee holding options or rights to acquire in excess of 5% of the issued and outstanding common shares (on a non-diluted basis). The Committee may suspend, amend, or terminate the 1998 Plan at any time without notice, provided that no outstanding option is adversely affected thereby. The further approval of the Company's shareholders is required only for amendments that increase the number of shares available for issuance under the 1998 Plan, that materially increases the benefits accruing to participants, or that materially changes the class of persons eligible for the granting of options. The 1998 Plan will automatically terminate on February 10, 2003, unless it has previously been terminated by the Committee, but options granted before the termination of the 1998 Plan may be exercised until they expire in accordance with their original term. At December 31, 1998, options to purchase an aggregate total of 708,620 common shares had been granted under the 1998 Plan of which 703,770 were outstanding and are exercisable in the future at prices ranging between $18.55 and $27.55 per common share.

Note 6.

Share Capital (continued)

Stock option information with respect to all of the Company's stock option plans is presented below:

	Shares	Price Range
Outstanding at January 1, 1996	1,376,841	$ 5.50 – 11.13
Granted	562,890	13.50 – 27.00
Exercised	(1,092,400)	5.50 – 24.00
Canceled	(55,287)	8.00 – 13.50
Outstanding at December 31, 1996	792,044	5.88 – 27.00
Granted	832,385	21.75 – 34.25
Exercised	(184,707)	5.88 – 31.85
Canceled	(9,367)	8.75 – 31.85
Outstanding at December 31, 1997	1,430,355	8.75 – 34.25
Granted	1,158,244	18.55 – 27.55
Exercised	(161,890)	9.00 – 21.75
Canceled	(45,040)	10.88 – 34.25
Outstanding at December 31, 1998	2,381,669	$ 8.75 – 34.25

The number of options issued and outstanding under all plans at any time is limited to 10% of the number issued and outstanding common shares of the Company. As of December 31, 1998 the number of options issued and outstanding under all plans was less than 9% of the issued and outstanding common shares.

Options outstanding at December 31, 1998 have expiration dates up to December 15, 2003 at a weighted average exercise price of $23.85 per common share. At December 31, 1998, stock options to purchase 1,807,377 common shares were exercisable. See Note 13(a) – Subsequent Events.

(d) Warrants

In relation to a 1995 licensing agreement, an affiliate of CIBA Vision received a common share purchase warrant to purchase 500,000 common shares of the Company until March 21, 1999 at an escalating exercise price to a maximum of $8.82 per share effective March 22, 1998. As at December 31, 1998, the common share purchase warrants had not been exercised. See Note 13(b) – Subsequent Events.

As part of a private placement of the Company's common shares on December 18, 1996, Beaufour Ipsen received a common share purchase warrant to purchase 197,863 common shares for U.S.$5,000,000 – U.S.$25.27 per share – (approximately $7,667,000 – $38.75 per share) anytime prior to December 18, 1999. As of December 31, 1998, the common share purchase warrant had not been exercised.

Note 7. Collaborative Arrangements

(a) CIBA Vision Ophthalmics AG (CIBA Vision)

During 1995, the Company entered into an agreement with CIBA Vision for the joint development and marketing of the Company's products as potential treatments for certain eye diseases. The Company is responsible for 40% of the research and development costs and CIBA Vision is responsible for the remaining 60%. The Company and CIBA Vision will share equally the profits realized on revenues from product sales. As part of a separate licensing agreement, an affiliate of CIBA Vision received a common share purchase warrant to purchase 500,000 common shares of the Company in exchange for the licensing to the Company of certain product and intellectual property rights, see Note 6(d) – Share Capital.

(b) Sanofi Pharmaceuticals, Inc. (Sanofi)

On January 9, 1996, the Company entered into an agreement with Sanofi with respect to the marketing of the Company's products in the United States and the Caribbean for cancerous and precancerous conditions.

In consideration for these rights, Sanofi will provide up to U.S.$21,500,000 in access fees and milestone payments to the Company. The Company is also entitled to receive reimbursement of manufacturing costs and royalty payments based on product sales by Sanofi. During 1998, 73% of total royalty revenue was attributable to product sales by Sanofi (1997 – 73%, 1996 – 61%).

As of December 31, 1998, the Company has received an access fee of U.S.$5,000,000 ($6,800,000) which was
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Lee Anne Pilson
Vice President, Marketing

Note 6.

Share Capital (continued)

Stock option information with respect to all of the Company's stock option plans is presented below:

	Shares	Price Range
Outstanding at January 1, 1996	1,376,841	$ 5.50 – 11.13
Granted	562,890	13.50 – 27.00
Exercised	(1,092,400)	5.50 – 24.00
Canceled	(55,287)	8.00 – 13.50
Outstanding at December 3		
Granted		
Exercised		
Canceled		
Outstanding at December 3		
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Outstanding at December 3		

The number of options issue
outstanding common shares
under all plans was less tha

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(d) Warrants

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Lee Anne Pilson
Vice President, Marketing

Before joining QLT as head of marketing in 1992, Ms. Pilson had 13 years experience in marketing, new products planning, and medical communications with leading pharmaceutical companies and agencies based in the U.S. QLT's marketing department has since grown to seven people with 70 years of combined work experience in some 20 therapeutic areas and multiple jurisdictions.

The team has expertise in all areas of marketing including new product planning, market research, product launches, sales, medical education and communication, and business development – functions that are increasingly critical as QLT evolves into a significant commercial entity.

"The marketing function at QLT is not a traditional one since we don't directly sell our own products. Instead, our job is to ensure that our partners maximize their opportunities by leveraging the expertise we have in photodynamic therapy. Our emphasis is on marketing development, management, and strategic planning."

"Our primary focus in 1999 is to work with CIBA Vision to maximize the global launch and commercialization of Visudyne™ for wet AMD. We will also continue to work on expanding the market for our cancer product, PHOTOFRIN, while providing input and direction for new product opportunities. Our future looks very exciting."

Note 7. Collaborative Arrangements

(a) CIBA Vision Ophthalmics AG (CIBA Vision)

During 1995, the Company entered into an agreement with CIBA Vision for the joint development and marketing of the Company's products as potential treatments for certain eye diseases. The Company is responsible for 40% of the research and development costs and CIBA Vision is responsible for the remaining 60%. The Company and CIBA Vision will share equally the profits realized on revenues from product sales. As part of a separate licensing agreement, an affiliate of CIBA Vision received a common share purchase warrant to purchase 500,000 common shares of the Company in exchange for the licensing to the Company of certain product and intellectual property rights, see Note 6(d) – Share Capital.

(b) Sanofi Pharmaceuticals, Inc. (Sanofi)

On January 9, 1996, the Company entered into an agreement with Sanofi with respect to the marketing of the Company's products in the United States and the Caribbean for cancerous and precancerous conditions.

In consideration for these rights, Sanofi will provide up to U.S.$21,500,000 in access fees and milestone payments to the Company. The Company is also entitled to receive reimbursement of manufacturing costs and royalty payments based on product sales by Sanofi. During 1998, 73% of total royalty revenue was attributable to product sales by Sanofi (1997 – 73%, 1996 – 61%).

As of December 31, 1998, the Company has received an access fee of U.S.$5,000,000 ($6,800,000) which was earned and recorded in 1996 and paid in 1997. Based upon the occurrence of certain future events, the Company is entitled to additional milestone payments of U.S.$16,500,000.

Under the terms of the 1996 agreement, Sanofi purchased 368,069 non-transferable convertible redeemable Series D First Preference Shares issued at a price of U.S.$13.58 ($18.47) per share for total proceeds of U.S.$5,000,000 ($6,850,000). The Series D First Preference Shares are redeemable in full by the Company prior to January 1, 2000 for cash and convertible in full by Sanofi after January 1, 2000 into common shares of the Company each according to a formula. The share purchase agreement between the Company and Sanofi provides for additional redemption or conversion rights for each party upon certain events including material breach or termination of the U.S. marketing agreement between Sanofi and the Company.

(c) Beaufour Ipsen Group (Beaufour Ipsen)

On December 18, 1996, the Company entered into an agreement with Beaufour Ipsen for the marketing of the Company's products in Europe for cancerous and precancerous conditions.

In consideration for these rights, Beaufour Ipsen will provide up to U.S.$28,000,000 in access fees, milestone payments and minimum research and development funding commitments to the Company. The Company will be responsible for manufacturing and Beaufour Ipsen will pay the Company a royalty on product sales plus a manufacturing transfer price.

As of December 31, 1998, the Company has received U.S.$4,000,000 ($5,489,986) of access fee and milestone payments (1997 – U.S.$2,000,000 ($2,789,986), 1996 – U.S.$2,000,000 ($2,700,000)) as well as received or earned U.S.$2,595,000 ($3,852,000) of research and development funding (1998 – U.S.$1,978,000 ($2,972,000), 1997 – U.S.$617,000 ($880,000)). Based upon the occurrence of certain future events the Company is entitled to additional aggregate payments of U.S.$21,405,000.

Under the terms of the 1996 agreement, Beaufour Ipsen purchased, on a private placement basis, 197,863 common shares of the Company at a price of U.S.$25.27 ($34.11) per common share, for a total equity investment of U.S.$5,000,000 ($6,750,000), representing a 33% premium-to-market price and subject to a two year hold period. Beaufour Ipsen has received a common share purchase warrant to purchase an additional 197,863 common shares, see Note 6(d) – Share Capital.

Note 7.
Collaborative
Arrangements (continued)

(d) C.R. Bard (Bard)

On April 30, 1998, the Company announced the formation of a strategic alliance with Bard to develop a therapeutic system and procedure for the reduction of arterial restenosis utilizing localized delivery of photodynamic therapy (QLT-Bard Alliance). Under the terms of the partnership, Bard will fund product development and clinical research and market the final products on an exclusive world-wide basis. QLT is entitled to receive royalty payments from Bard and has retained an option to co-fund research and development at a later date in exchange for an increased share of sales revenue. This agreement has not had a material effect on research and development costs for 1998 nor is it expected to in 1999.

On September 30, 1998, Bard finalized an agreement to sell certain of its businesses, products and technologies that comprise its coronary catheter laboratory business to AVE (Bard-AVE Transaction). Under the terms of the Company's agreement with Bard, Bard has the right to assign its rights and obligations under the agreement in connection with the sale of all or a substantial portion of Bard's cardiology related assets. Although pre-clinical work is being carried out by AVE, as of the date of this report, the Company has not received formal written notification by Bard that it has exercised its rights of assignment under the QLT-Bard Alliance in connection with the Bard-AVE Transaction.

(e) Ligand Pharmaceuticals Inc. (Ligand)

During 1995, the Company entered into a marketing and distribution agreement with Ligand for the exclusive distribution of PHOTOFRIN in Canada. Under the terms of the ten year agreement, the Company will supply PHOTOFRIN to Ligand and Ligand and the Company will share revenues from product sales based on a formula provided for in the agreement. Ligand paid the Company an initial licensing fee in 1995 and is obligated to make three fixed payments in the future based on the attainment of certain cumulative net product sales levels.

(f) American Home Products Corporation (American Home)

In 1987, Cyanamid entered into a co-development and distributorship agreement with the Company. In November 1994, American Home acquired indirectly all of the outstanding common shares of Cyanamid, which continues to operate as a wholly-owned subsidiary of American Home. As of December 31, 1997, American Home was the beneficial owner of less than 5% of the issued and outstanding common shares of the Company.

During the last three fiscal years, the Company had the following related party transactions with American Home or Cyanamid:

(i) During 1998, the Company contracted the services of American Home in the development and manufacturing of PHOTOFRIN and verteporfin on a basis consistent with terms and conditions for the provision of such services between unrelated parties for total fees of $858,000 (1997 – $631,000; 1996 – $309,000).

(ii) During 1996, the Company reacquired certain product rights to PHOTOFRIN from American Home for total purchase consideration of approximately $500,000 including the estimated cost of transferring such rights.

(iii) Effective December 1, 1996, the Company and various affiliates of American Home entered into three new agreements relating mainly to the continued manufacture and distribution of PHOTOFRIN in Japan by American Home.

Note 8.
Income Taxes

The Company has approximately $7,132,000 of research and development expenditures available for unlimited carry forward, approximately $8,793,000 of non-capital losses expiring between 1999 and 2005, and approximately $334,000 of unclaimed investment tax credits expiring in 1999, all of which may be used to reduce future Canadian income taxes otherwise payable. In addition, the Company has approximately U.S. $90,414,000 of net operating losses expiring between 2002 and 2018 which may be used to reduce future U.S. income taxes otherwise payable. The timing and manner in which these losses may be used could be limited as a result of certain ownership changes which may occur as provided under U.S. tax legislation. Recognition of the potential tax benefits associated with these items has not been reflected in the financial statements.

Note 9.
Financial Instruments and Concentration of Credit Risk

As at December 31, 1998, the carrying amounts reported in the balance sheet for cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities approximate fair value, due to the short term nature of these instruments. The carrying values of short and long-term investments also approximate fair value. With respect to accounts receivable, the total amount due for reimbursement of co-development costs represents the aggregate owing from the Company's two co-development partners. The Company purchases goods and services in both Canadian and U.S. dollars and earns a significant portion of its revenues in U.S. dollars. Foreign exchange risk is managed by satisfying foreign denominated expenditures with cash flows or assets denominated in the same currency. The Company has not entered into forward currency contracts or other financial derivatives to hedge exchange risk.

Note 10.
Commitments

(a) Lease Commitments

The Company leases office and laboratory space under non-cancellable operating leases which all expire on September 30, 1999. Minimum future rental commitments for these leases are $490,000. The Company is also responsible for its proportionate share of operating costs under the leases. During the year ended December 31, 1998, total rent expense was $1,244,000 (1997 – $915,000; 1996 – $952,000).

(b) New Facility Under Construction

The Company has commenced the construction of its new office and research facility in Vancouver, B.C. Completion of construction and occupancy is expected by late 1999. Total project cost, including land and capitalized financing and other soft costs, is expected to be approximately $22 million. As at December 31, 1998, $4.1 million had been expended or incurred on this project. The Company has entered into a fixed price construction contract for the base building in the amount of $16,085,000, of which $705,901 for the first progress claim was accrued at year end. The Company has secured a commitment from a major Canadian financial institution to provide up to $15.6 million of interim construction financing, which upon completion of construction would be replaced by a fixed rate term loan of $14 million.

(c) Royalties

The Company is also responsible for payment of royalties to unrelated third parties on certain product sales. These royalty arrangements are on reasonable commercial terms and are in the ordinary course of business in the pharmaceutical industry.

Note 11.
Differences Between Canadian and United States Generally Accepted Accounting Principles

(a) Accounting for Certain Investments in Debt and Equity Securities

In May 1993, the Financial Accounting Standards Board (FASB) in the United States issued Statement of Financial Accounting Standards No. 115, "Accounting for Certain Investments in Debt and Equity Securities" (SFAS 115). Under SFAS 115, management determines the appropriate classification of investments in debt and equity securities at the time of purchase and re-evaluates such designation as of each balance sheet date. Under SFAS 115, the Company would classify its short-term and long-term investments as available-for-sale securities, which are to be carried at fair value, with unrealized gains and losses reported as a separate component of shareholders' equity. If the Company had adopted SFAS 115, the effect on shareholders' equity and net loss would not have been material for any of the three years ended December 31, 1998.

(b) Accounting for Income Taxes

Under U.S. GAAP, the Company is required to account for income taxes in accordance with the provisions of Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" (SFAS 109). SFAS 109 requires deferred tax assets or liabilities to be recorded for temporary differences that will result in deductible or taxable amounts in future years as well as loss carry-forwards and deferred investment tax credits. A valuation allowance would be recorded for the portion of the asset where the realization of any value is uncertain. Both the deferred tax asset and valuation allowance have been valued at $56,074,000 as at December 31, 1998 ($47,019,000 as at December 31, 1997).

(c) Accounting for Stock Based Compensation

Under U.S. GAAP, in accordance with Statement of Financial Accounting Standards No. 123, "Accounting for Stock Based Compensation" (SFAS 123), the Company is required to either disclose or recognize stock based compensation costs using the fair value method. Under Canadian GAAP, the fair value of stock based compensation costs, using either the intrinsic or fair value methods, is not recognized or disclosed in the financial statements. The following unaudited pro forma financial information presents the net loss and loss per common share had the Company adopted SFAS 123.

Year ended December 31, (In thousands except per share information)	1998	1997	1996
Net loss			
As reported	$ 24,071	$ 16,683	$ 4,697
Pro forma	37,104	27,062	10,674
Net loss per common share			
As reported	$ 0.90	$ 0.64	$ 0.19
Pro forma	1.39	1.04	0.44

The pro forma amounts may not be representative of future disclosures since the estimated fair value of stock options is amortized to expense over the vesting period and additional options may be granted in future years.

The weighted average fair value of stock options granted during 1998 was calculated to be $15.29 (1997 – $14.72, 1996 – $12.31) using the Black-Scholes option pricing model. The calculated fair value may not be indicative of the actual amount realized upon the exercise of the stock options by the holders. The weighted average assumptions used in the model were as follows: volatility factor for the Company's share price of 53%, (1997 – 50%; 1996 – 77%); risk-free interest rate of 5.0% (1997 – 6.0%; 1996 – 5.40%); and no payment of dividends on common shares.

(d) Earnings Per Share

In February 1997, the FASB issued Statement of Financial Accounting Standards No. 128, "Earnings per Share" (SFAS 128). SFAS 128 redefines earnings per share under U.S. GAAP and replaces primary earnings per share with basic earnings per share and fully diluted earnings per share with diluted earnings per share. Net loss per share, as reported for all years presented, is equal to the net basic and diluted loss per share as prescribed by SFAS 128.

(e) Reporting Comprehensive Income

In June 1997, the FASB issued Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income" (SFAS 130). SFAS 130 establishes standards for reporting comprehensive income and its components in a set of general-purpose financial statements that is displayed with the same prominence as other financial statements. Comprehensive income, as defined, includes all changes in equity (net assets) during a period from non-owner sources, including for example, unrealized gains or losses on short-term investment securities which are currently excluded from the results of operations. The prescribed disclosures, do not have a material effect on the financial statements.

Dr. David Dolphin, Ph.D
Vice President, Technology Development

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Dr. David Dolphin, Ph.D
Vice President, Technology Development

Dr. David Dolphin is a world-renowned expert in porphyrin chemistry and biochemistry. His many awards include a Gold Medal from the Science Council of British Columbia; the Syntex Award of the Canadian Institute of Chemistry; the Bell-Canada Forum Award; the Isaac Walton Killam Research Prize and a Guggenheim Fellowship.

Dr. Dolphin combines his work at QLT with a Professorship in Chemistry at the University of British Columbia, where he co-discovered the family of photosensitive compounds that led to the development of verteporfin, QLT's product for age-related macular degeneration.

On behalf of QLT, Dr. Dolphin serves as a key spokesperson with the FDA and other regulatory bodies regarding chemistry and manufacturing issues. He is the author of 18 books on spectroscopy, chemistry and biochemistry, and has published over 350 research papers.

"In our quest to identify new and unique photosensitizers, we try to refine specific properties which make a particular drug more amenable to treating certain disease groups. We also try to improve on the synthesis of each compound in order to optimize the manufacturing processes. Our chemistry group has the ability to synthesize virtually any porphyrin-related system, securing our competitive lead for years to come."

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In February 1997, the FASB issued Statement of Financial Accounting Standards No. 128, "Earnings per Share" (SFAS 128). SFAS 128 redefines earnings per share under U.S. GAAP and replaces primary earnings per share with basic earnings per share and fully diluted earnings per share with diluted earnings per share. Net loss per share, as reported for all years presented, is equal to the net basic and diluted loss per share as prescribed by SFAS 128.

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(f) Recent Accounting Pronouncements

In June 1998, the FASB issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" (SFAS 133). SFAS 133 establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities. SFAS 133 is effective for fiscal years beginning after June 15, 1999 and its impact has not been determined.

Note 12. Uncertainty Due to the Year 2000 Issue

The Year 2000 Issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using year 2000 dates is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date. The effects of the Year 2000 Issue may be experienced before, on, or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant systems failure which could affect a company's ability to conduct normal business operations. It is not possible to be certain that all aspects of the Year 2000 Issue affecting the Company, including those related to the efforts of customers, suppliers, or other third parties, will be fully resolved.

Note 13. Subsequent Events

Subsequent to December 31, 1998, the Company:

(a) received $14,346,434 from the issuance of 621,445 common shares pursuant to the exercise of employees' options at exercise prices between $8.75 and $34.25 per common share.

(b) received $4,410,000 from the issuance of 500,000 common shares pursuant to the exercise of a common share purchase warrant, by a CIBA Vision affiliate, at an exercise price of $8.82 per common share.

Stock Market Information

The Common Shares of the Company trade in Canada on The Toronto Stock Exchange under the symbol "QLT" and in the United States on The Nasdaq Stock Market under the symbol, "QLTI", "QLTIF" prior to February 26, 1999. The Company has not paid cash dividends on its Common Shares since its inception and does not anticipate doing so in the foreseeable future. The Company intends to retain future earnings, if any, and capital for use in the expansion of its business. The following table sets forth, for the periods indicated, the high and low closing sales prices and trading volume of the Common Shares, as reported by The Toronto Stock Exchange and The Nasdaq Stock Market.

	The Toronto Stock Exchange			The Nasdaq Stock Market (U.S.$)		
	High	Low	Volume	High	Low	Volume
1998						
First Quarter	$ 26.20	$ 15.90	7,229,696	$ 18.75	$ 11.06	1,754,400
Second Quarter	29.25	23.05	3,325,463	19.63	16.00	1,664,700
Third Quarter	26.00	17.70	3,684,210	17.69	11.75	1,771,300
Fourth Quarter	38.00	16.50	4,986,949	27.63	10.80	3,215,800
1997						
First Quarter	$ 39.00	$ 27.25	8,344,121	$ 28.63	$ 19.81	4,205,150
Second Quarter	35.75	27.60	5,309,762	25.63	19.88	1,942,992
Third Quarter	30.55	21.85	9,709,827	22.00	15.75	4,026,830
Fourth Quarter	26.00	15.25	5,757,273	18.69	10.75	3,142,600

The last reported sale price of the Common Shares on The Toronto Stock Exchange and on The Nasdaq Stock Market on February 26, 1999, was $58.70 and U.S.$39.00, respectively.

As of February 26, 1999, there were 527 registered holders of the Common Shares of the Company, 307 of whom were residents of the United States. Of the total 28,385,597 Common Shares outstanding, the portion held by residents of the United States was 7,490,593 or 24.8%.

Selected Financial Information

Annual Financial Data

Set forth below is selected consolidated financial data for, and as of the end of, each of the years in the five year period ended December 31, 1998, derived from the consolidated financial statements of the Company that have been audited by Deloitte & Touche LLP. The information below is not necessarily indicative of the results of future operations and should be read in with Management's Discussion and Analysis of Financial Condition and Results of Operations, and the Consolidated Financial Statements and Notes thereto.

Year Ended December 31 (In thousands of Canadian Dollars except per share information)	1998	1997	1996	1995	1994
Consolidated Statement of Operations Data					
Total revenues	$ 7,575	$ 10,341	$ 13,497	$ 2,531	$ 3,776
Research and development costs	23,890	19,214	11,480	12,068	13,846
Net loss	24,071	16,683	4,697	14,690	14,276
Net loss per common share	0.90	0.64	0.19	0.77	0.72
Consolidated Balance Sheet Data					
Cash, cash equivalents and investment securities	$ 78,245	$ 89,788	$ 97,151	$ 16,057	$ 30,515
Working capital	85,152	87,794	104,487	12,277	24,060
Total assets	103,223	101,223	112,195	22,678	37,513
Shareholders' equity	95,078	94,848	108,857	21,194	33,765

Quarterly Financial Data

Set forth below is selected unaudited consolidated financial data for the fiscal quarters of 1998 and 1997.

Three Months Ended (In thousands of Canadian Dollars except per share information)	March 31	June 30	September 30	December 31
1998				
Total revenues	$ 2,052	$ 1,575	$ 1,949	$ 1,999
Research and development costs	5,427	5,143	5,880	7,440
Net loss	4,959	5,274	6,355	7,483
Net loss per common share	0.19	0.20	0.24	0.27
1997				
Total revenues	$ 2,052	$ 1,373	$ 2,590	$ 4,326
Research and development costs	2,754	4,924	4,828	6,708
Net loss	2,467	5,746	3,723	4,747
Net loss per common share	0.10	0.22	0.14	0.18

Corporate Directory

Directors

E. Duff Scott [2, 4]
President, Multibanc NT Financial Corp.

Peter A. Crossgrove [1, 3]
Director, Dundee Realty Corporation

Jan Dlouhy Ph.D. [2]
Retired Vice President, Licensing and Acquisitions, Medical and Agricultural Groups, American Cyanamid Company

Robert J. Feeney Ph.D. [2, 3]
Retired General Partner, Hambrecht and Quist Life Science Technology Fund

Anthony F. Griffiths [1]
Corporate Director

Ronald D. Henriksen [1, 3]
President, Advanced Research & Technology Institute, Indiana University

Julia G. Levy Ph.D.
President and Chief Executive Officer, QLT PhotoTherapeutics Inc.

Senior Management

Julia G. Levy Ph.D.
President and Chief Executive Officer

Kenneth H. Galbraith C.A.
Senior Vice President, Chief Financial Officer and Corporate Secretary

Mohammad Azab M.D.
Vice President, Clinical Research and Medical Affairs

David Dolphin Ph.D.
Vice President, Technology Development

Edwin Levy Ph.D.
Vice President, Corporate Development

Alexandra Mancini
Vice President, Regulatory Affairs

John R. North Ph.D.
Vice President, Scientific Affairs & Chief Scientific Officer

Lee Anne Pilson
Vice President, Marketing

[1] Member of the Audit Committee, Chair: Anthony F. Griffiths
[2] Member of the Nominating Committee, Chair: E. Duff Scott
[3] Member of the Executive Compensation Committee, Chair: Peter A. Crossgrove
[4] Chairman of the Board of Directors

Corporate Headquarters

QLT Place, 520 West 6th Avenue
Vancouver, British Columbia
Canada V5Z 4H5
Telephone: (604) 872-7881
Fax: (604) 875-0001
www. qlt-pdt.com

Register and Records Office

Farris, Vaughan, Wills & Murphy
2600 – 700 West Georgia Street
Vancouver, British Columbia
Canada V7Y 1B3

Transfer Agent and Registrar Office

Montreal Trust Company
Stock and Bond Transfer Department
510 Burrard Street
Vancouver, British Columbia
Canada V6C 3B9
For change of address, lost stock certificates and other related inquiries, please write to the above address.

Independent Auditors

Deloitte & Touche LLP, Vancouver, Canada

Stock Listing

The Company's Common Shares are traded on the Toronto Stock Exchange under the symbol QLT and on The Nasdaq Stock Market under the symbol QLTI.

Form 10-K Annual Report

A copy of the Company's Form 10-K Annual Report, as filed with the Securities and Exchange Commission, is available on our website www.qlt-pdt.com or upon request from:
QLT PhotoTherapeutics Inc.
Investor Relations Department
QLT Place, 520 West 6th Avenue
Vancouver, British Columbia
Canada V5Z 4H5

Annual Meeting

The Annual Meeting of Shareholders will be held at the Waterfront Centre Hotel, Vancouver, at 10:00 a.m. on Tuesday, May 4, 1999.

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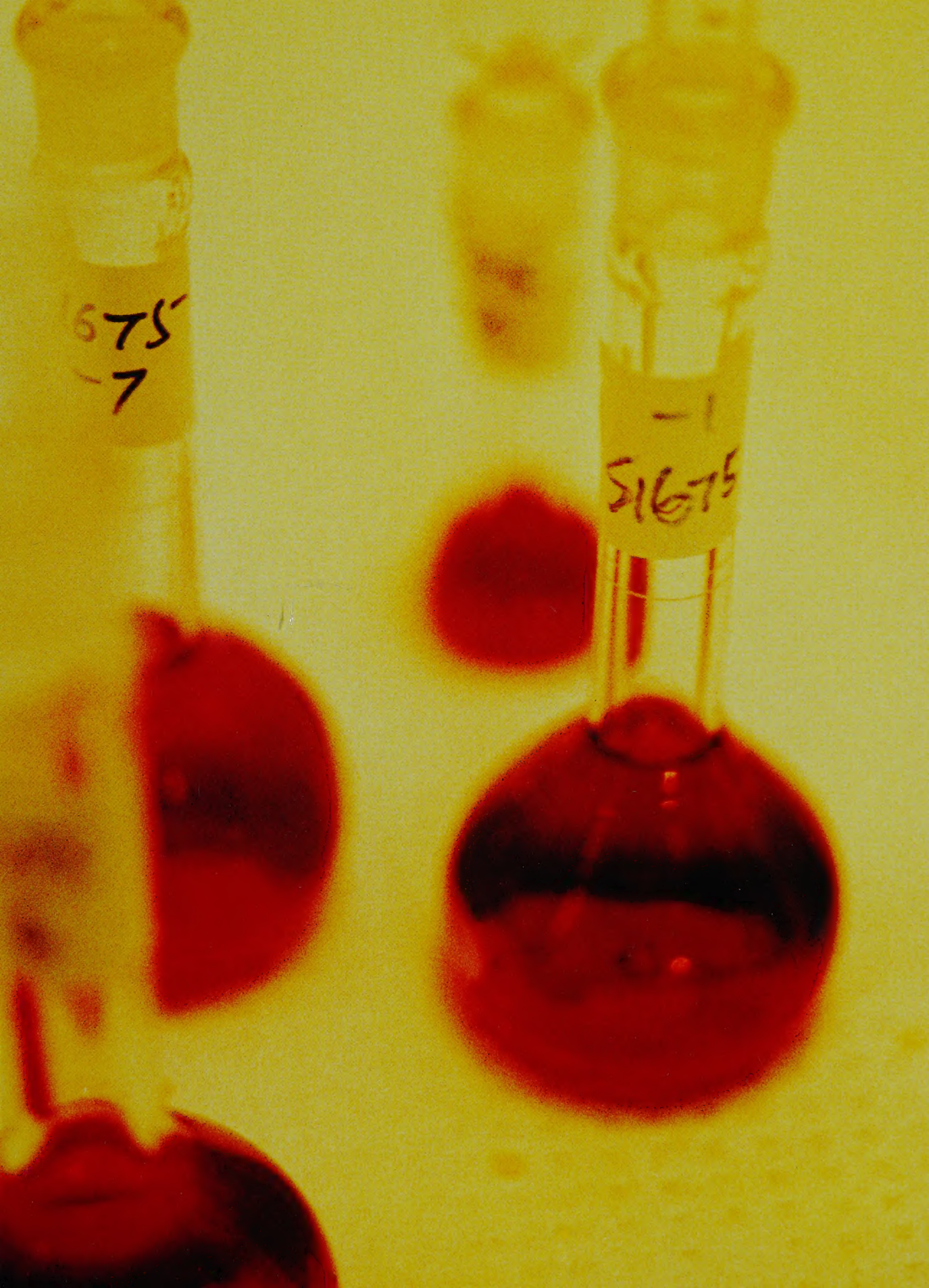
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1998 Annual Report